

The CEO and the audit committee

Introduction

On June 10, 2008, members of the Audit Committee Leadership Network (ACLN) met in New York for the network's 17th stand-alone meeting. During private sessions, members discussed the process of selecting a new audit partner and the importance of working collaboratively during this process with the audit firm. Members also discussed board-shareholder communication¹ and the consequences of the credit crisis. Notes from the latter discussion can be found in the appendix on page 10. For further information about the network, see "About this document," on page 9.

During their discussion on the CEO and the audit committee, members focused on:

- **The optimal relationship between the audit committee and the CEO**
- **CEO engagement with the audit committee and the external auditor**
- **The audit committee's role in supporting good tone at the top**

Audit chairs participating in the meeting, who sit on the boards of about 25 large-, mid-, and small-cap public companies between them, included:

- Denny Beresford, Audit Committee Chair, Kimberly-Clark
- Dick Harrington, Audit Committee Chair, Xerox
- Judith Richards Hope, Audit Committee Chair, Union Pacific
- Labe Jackson, Audit Committee Chair, JPMorgan Chase
- Mike Losh, Audit Committee Chair, Cardinal Health
- Sandy Warner, Audit Committee Chair, General Electric Company
- Steve West, Audit Committee Chair, Cisco Systems
- Chris Williams, Audit Committee Chair, Wal-Mart

Members from Ernst & Young participating in the meeting were:

- Steve Almassy, Americas Assurance Leader
- Steve Howe, Americas Managing Partner

ViewPoints reflects the network's use of a modified version of the Chatham House Rule whereby names of members and their company affiliations are a matter of public record, but comments made before and during meetings are not attributed to individuals or corporations.

¹ See Audit Committee Leadership Network, "Board-shareholder communication," *ViewPoints*, July 7, 2008. Available at http://www.tapestrynetworks.com/documents/Tapestry_EY_ACLN_Jul08_View22.pdf.

Executive summary

During their discussion on the CEO and the audit committee, members focused on the following topics, which are covered in more detail on the following pages:

- **The optimal relationship between the audit committee and the CEO** (*Page 2*)

Members discussed the personal relationship that they have with their CEOs, describing the need to remain at arm's length in order to maintain independence. Members outlined factors that contribute to a strong relationship with the CEO: trust in both directions (with their own comportment being important to avoid a “gotcha” environment), regular and candid communication, and CEO support of the audit chair's open communication with others in the company. Audit chairs who were former CEOs reported that they often acted as advisers to their CEO.

- **CEO engagement with the audit committee and the external auditor** (*Page 6*)

CEO attendance at audit committee meetings varies from company to company. Members report a wide range of practice: some CEOs attend all audit committee meetings; some attend only occasionally; some generally do not attend. Members note that audit chairs should be aware of the way in which the CEO's presence affects meeting dynamics and should seek to mitigate that change by taking charge of the meeting and being prepared to push back on the CEO if necessary.

Members generally supported the notion of a relationship between the lead audit partner or review partner and the CEO, as long as that relationship is valuable to the CEO. A three-way relationship between the CEO, the audit partner, and the audit chair can help all three calibrate their perspectives. Some members also encourage their CEO to develop a relationship with the audit firm's leadership for a broader perspective on the profession.

- **The audit committee's role in supporting good tone at the top** (*Page 8*)

Members described how the CEO sets tone at the top through a combination of consistent words and actions and the swift punishment of violations. Members agreed that the audit committee cannot drive tone at the top but can support it by interacting with employees through regular site visits, spending time with the CEO's direct reports, being accessible to finance and internal audit staff, reviewing employee survey data, and providing guidance to the CEO on dealing with any lapses.

The optimal relationship between the audit committee and the CEO

As the *Chief Executive* noted in 2003, “The classic CEO management mode – distant and hierarchical – is losing out to a new style that's more open, communicative and collaborative.”² A 2007 Booz Allen Hamilton study found that boards are now more deeply engaged in setting strategy and less tolerant of poorly

² Justin Martin, “Rise of the new breed: the age of the imperial CEO is waning,” *Chief Executive*, August–September 2003. Available at http://findarticles.com/p/articles/mi_m4070/is_191/ai_109669774.

performing CEOs. That study found that “inclusiveness is the most critical new attribute for the CEO.”³ The average tenure of a CEO is also declining.⁴

More inclusiveness on the part of CEOs has coincided with the audit committee’s enhanced role in overseeing company financial statements. Sarbanes-Oxley Section 302 (Corporate Responsibility for Financial Reports) necessitated greater involvement of the CEO to certify his or her evaluation of the financial statements and the effectiveness of internal controls. Section 404, which focuses on internal controls, often required similar increased involvement with the audit committee.

Taken together, these requirements increased the complexity of the audit committee’s relationship with the CEO. On the one hand, the audit committee and the CEO need to work collegially to ensure the quality of internal controls. On the other hand, the audit committee has to oversee senior management to assure the accuracy of financial statements and the processes used to assess and manage risks. Members agreed it was an appropriate time to reassess the nature of the audit committee’s – and particularly the audit chair’s – relationship with the CEO.

Gaining and keeping trust

At the first in-person meeting of the ACLN in September 2003, members described their relationship with their CEOs in terms of President Reagan’s dictum regarding negotiation with the Soviet Union: “Trust, but verify.”⁵ In 2005, Richard Steinberg wrote in *Compliance Week* that “another term that’s come into vogue among audit committee circles, ‘constructive skepticism,’ may be more appropriate.”⁶

At the June 2008 meeting, members described their personal relationships with their CEOs. One member characterized the relationship as “*cordial, but somewhat distant,*” saying the distance was necessary in order to maintain independence. Another member said, “*My CEO and I don’t have a close personal relationship, but we know each other, and I know how he will react, and he knows how I will react on any issue. It is valuable to me and to him.*”

The NACD’s Blue Ribbon Commission on audit committees noted, “Management’s attitude toward the audit committee is of paramount importance. If the CEO and senior managers are not completely supportive of the audit committee’s purpose, composition, and process, the committee may be unable to fulfill its responsibilities successfully.”⁷ One member commented, “*It requires trust both ways. The audit*

³ Chuck Lucier, Steven Wheeler, and Rolf Habel, “The Era of the Inclusive Leader,” *strategy+business*, no. 47 (Summer 2007), 12. Available at http://www.boozallen.com/media/file/Era_of_the_Inclusive_Leader_.pdf.

⁴ The National Bureau of Economic Research reports that in the period from 1998 through 2005, total CEO annual turnover was 16.5%, implying an average tenure of just over six years, compared with a turnover rate of just 10% in the 1970s and 11% in the 1980s. Steven N. Kaplan and Bernadette A. Minton, *How Has CEO Turnover Changed: Increasingly Performance Sensitive Boards and Increasingly Uneasy CEOs* (Washington, DC: National Bureau of Economic Research, 2006), 1. Research available at <http://faculty.chicagogsb.edu/steven.kaplan/research/km.pdf>.

⁵ Audit Committee Leadership Network, “Audit committee emerging roles and responsibilities,” *ViewPoints*, October 15, 2003, 2. Available at http://www.tapestrynetworks.com/documents/Tapestry_EY_ACLN_Oct03_View2.pdf.

⁶ Richard Steinberg, “How Audit Committees Best Carry Out Responsibilities,” *Compliance Week*, May 24, 2005. Available to subscribers at http://www.complianceweek.com/index.cfm?fuseaction=article.SavedSearchResults&search_ID=82.

⁷ National Association of Corporate Directors, *Report of the Blue Ribbon Commission on Audit Committees: A Practical Guide – Updated 2004 Edition* (Washington DC: National Association of Corporate Directors, 2004), 13.

chair must trust the CEO totally. And it needs huge respect both ways. The CEO needs to acknowledge the criticality of the audit committee's role. It's not just a governance role: it is about assuring the criticality of the financials that keep the company afloat."

Other members agreed and pointed to the influence the CEO can have on the audit committee's ability to interact successfully with other managers in the company: *"The audit committee touches so many parts of the company now, and the CEO has to endorse ... [direct] communication with management in order for the audit committee to do the job. Signals from the CEO are important, so that others will understand the importance of the audit committee."* Another member commented, *"There is no wall between the audit committee and anyone in the organization. I still hear in some [small, public] companies the CEO needs to act as a filter. That is dangerous. You can't have communications go through the CEO."*

Audit chairs must work hard to ensure that once gained, trust is not lost – and their own behavior is an important factor: *"If you do something that loses the trust of the CEO, or any of those guys, you have a real problem. You can't play 'gotcha.' One 'gotcha,' and you will lose all that trust."*

Several members provided advice on how to avoid losing trust. One member said, *"I try to make it clear that my job is a continuing education. While I'm on the job, I will keep digging. I will need a lot of time to understand the company and be helpful."* Another member said, *"When talking to the CEO or CFO as audit chair, I make sure they know they can tell me that I'm asking the wrong questions, [questions] that might not help me get where I need to go. [I ask them,] 'Am I wasting your time? Could there be a better way to go?' Often when the audit chair calls, the alarm bells go off."*

Regular and candid communication

Many members identified *"ongoing communication"* as an important factor in building trust: *"You want a phone call when something happens, not to hear about it at the next audit committee meeting. You can't build trust without being sure you are first to know. You want a 'no surprises' approach."* Another member commented, *"I call [the CEO] 60% of the time; [the CEO] calls me 40% [of the time]. If there's a problem, [the CEO] calls me 100% of the time."* A third member added, *"Candor is a very important part of being independent and building trust."*

All members agreed that access to the CEO is critically important to them as audit chair: *"It's tricky if you're not talking regularly, and then you have an issue and there is a need to talk. It can be a little awkward. The CEO needs to be available to the audit chair very quickly. If I called and the CEO didn't get back to me right away, I would be concerned."* Another member agreed: *"You don't need to talk every week, but you need a regular check-in, so if you catch a problem, you can go deal with it rather than ramping up communications just because there's an issue."*

One member suggested that regular communication with the CEO is a real advantage to the audit chair in part because of the effect the knowledge of that communication has on other people: *"I get immediate answers to my questions."* Other members pointed out that the relationship with the CEO is only one important relationship for the audit chair: *"The CEO sets the tone at the top, but he is only one person."*

You have to talk to internal audit, the CFO, the financial [people]. You have to look at the totality of the organization ... Your span is beyond one person."

Focusing on different types of relationship

Members who were former CEOs tended to report that they have more engagement with their CEO, often acting as an adviser on certain matters during weekly telephone calls. These members said that CEOs were generally looking for a partnership: *"If you are signing off on financial reports, you want to be a partner with the audit chair for the benefit of the whole company. You will use their experience, knowledge, and expertise."* Members who were not former CEOs, by contrast, tended to focus on building a good relationship with the CFO and other direct reports of the CEO. These two approaches are described in more detail below:

- **Present a useful value proposition to the CEO.** One member noted, *"A CEO has limited time, and they need to know where they can go to get help. They might go to the audit chair for help if it is valuable, not just because it is the right thing to do or because it is required in the governance handbook."* Another member had requested a discussion with the CEO to clarify expectations after taking on the audit chair role, but such dialogues do not always take place. For an example of a value proposition in an audit chair–CEO relationship, see the box below.
- **Work more directly with the CFO.** One member said, *"[As former CEOs,] you are more likely to talk to the CEO than I am. With my background, I am more inclined to talk to the CFO ... unless there is a crisis. I talk to the CEO a few times per quarter."* Another member agreed: *"Talking to the CEO once a quarter is appropriate for me ... If any more was required, I'd feel something was wrong. I can always pick up the phone, day or night."*

Regardless of the approach taken, one member advised, *"Always remember who you work for. I work for the shareholders. If you do what's best for them, you'll probably do it the right way."*

Example of a value proposition developed for one audit chair–CEO relationship:

"This is the stuff that creates a value proposition for [the CEO] and a relationship that benefits shareholders."

- **People issues.** *"On compensation decisions for division managers, [the audit chair can provide] input on whether [the manager is] running a tight ship or not ... It's also 'hire or fire' decisions, where you can influence the decision."*
- **Business strategy.** *"[The audit chair can offer advice on] the executability of strategy; if it's too far afield, or too complex, or leaves too many orphans, it won't work."*
- **External communication.** *"I provide coaching on analyst meetings, listen in [to the calls], and [then the CEO] asks how I think he did."*



CEO engagement with the audit committee and the external auditor

Thinking about their relationship with the CEO beyond personal interactions, members talked about how the CEO engages with the audit committee, particularly by attending all or part of the audit committee meeting (or not), and how the CEO engages with the external auditor.

The CEO's attendance at audit committee meetings

CEO attendance at audit committee meetings varies from company to company. Members report a wide range of practice: some CEOs attend all audit committee meetings; others attend only when particular items come up; still others generally do not attend at all, except at the request of the audit chair.

- **CEO attends every meeting.** One member reported, *“We had [a large number of] audit committee meetings last year. Our CEO attended every minute of every one of them. [The CEO] can’t imagine not attending ... We have world-class controllership process, and [the CEO] wants to own the process which is the foundation of the company he runs. He wants to understand it as we understand it.”* Another member said, *“At my company, we used to have only two committees, with compensation and audit meeting at the same time. [At the] impetus [of our new CEO], we ‘unlapped’ committee meetings, so [the CEO] could attend both.”* For reasons why CEOs may attend or may not attend audit committee meetings, see box below.
- **CEO attends a portion of the meeting.** One member mentioned that when *“the CEO went to all the meetings, [a new member of the audit committee] asked if the CEO could come to only a portion of the meeting as it created a difference [in meeting dynamics].”*
- **CEO attends once a year or not at all.** One member said, *“My CEO comes once a year for an executive session with the audit committee, because it is required. [The session] lasts between 15 minutes and one hour depending on the issues.”* Another member remarked, *“Our CEO feels that not attending the audit committee reinforces the independence of the audit committee. I feel that is a little over the top, but [the CEO] feels strongly about it.”*

Why some CEOs attend audit committee meetings:

- To understand tough, complex, or difficult risk- or accounting-related issues
- To promote dialogue among board directors, auditors, and management
- To signal the audit committee's importance to the company
- For personal development, particularly for new CEOs and those without financial backgrounds

Why other CEOs do not attend audit committee meetings:

- Scheduling conflicts involving board committee meetings
- Reliance on a post-meeting briefing from the CFO and/or audit chair
- Audit committee agenda is overly focused on detailed compliance issues
- Key issues will be discussed at the full board meeting anyway

The CEO's impact on committee meeting dynamics

Although audit chairs appreciate some level of CEO attendance at audit committee meetings for the interest and engagement it demonstrates, they also note that the CEO's presence may change the nature of the discussion. One said, *"I do see meeting [dynamics] change sometimes when the CEO comes."* Another commented that when the CEO *"stopped attending, the dynamics changed in the meeting. It's OK either way, but it did change."*

Those members whose CEOs attend all of every audit committee meeting were questioned about the impact. One member asked another, *"Do you worry [about the company's] people in the audit committee being frank and open with [the CEO] there?"* The response: *"Yes I do. I worry about it. Our general counsel is trying to find his way with the CEO."* A recent issue of *InSights* reported on a similar situation, quoting one general counsel who said, *"When you're at the board table, sometimes it's hard to be candid if your boss [the CEO] is [also] at the table."⁸*

One member said, *"If [the CEO] is there, I have to be willing to take charge as audit chair. If I disagree with him, I have to call him on it right there. It's your meeting, and your conclusions. It's part of the bargain [with the CEO] for coming to the meetings. If you don't push back, you aren't doing the job [the CEO] wants you to do."*

Relationships with the audit firm

The Sarbanes-Oxley Act significantly expanded the audit committee's responsibility for oversight of the company's relationship with the external auditor, which may lead the audit committee to consider what constitutes an appropriate relationship between the CEO and the external audit firm. Members discussed several different layers of the relationship:

- **Relationship with the lead audit partner.** Members generally supported a relationship between the lead audit partner and the CEO as long as there was a clear value proposition for the CEO. One member who is a former CEO reported benefiting from regular meetings with the lead audit partner, saying, *"It doesn't take long, and it doesn't hurt. It gives you another perspective. I did it for comfort. I [was] not doing it to check up on others. I wanted to know what [the external auditor] sees in our organization."* One audit chair commented, *"These meetings become significant three-way communications. Sometimes the stories don't match, and you need to get people on the same page. The audit chair can help."* Another member agreed: *"Let the CEO know you are meeting quarterly with the lead audit partner to calibrate judgments and gather perspectives."*

However, several members said that in their companies, the CEO does not meet with the lead audit partner. One said, *"My CEO doesn't do that. [The CEO] hears from the external auditor at the audit committee meeting and counts on me and the CFO to meet with them."*

⁸ Ernst & Young and Tapestry Networks, "The general counsel's perspective," *InSights*, February 6, 2008, 7. Available at http://www.tapestrynetworks.com/documents/Tapestry_EY_ACLN_InSights_Feb08.pdf.

- **Relationship with the review partner.** One member said the CEO meets regularly with the senior review partner on the account: *“The concurring partner talks to the CEO, CFO, and audit chair. It is actually incredibly helpful to me. We get into specific issues and future issues.”*
- **Relationship with audit firm leadership.** One member noted, *“If there is a negative PCAOB [Public Company Accounting Oversight Board] report, my CEO calls me to ask who [will be] ringing the firm to ask about it – him or me?”* Members suggested that it may be advantageous for CEOs to develop a relationship with the audit firm’s leaders, who have a broad perspective on both firm-wide and profession-wide issues.

The audit committee’s role in supporting good tone at the top

Some observers believe that the phrase “tone at the top” has begun to suffer from what psychologists call “semantic satiation” – loss of meaning that occurs when a word or phrase is overused.⁹ So how do members think about tone at the top? One member provided a pithy definition: *“Tone at the top is making sure everyone understands the rules of the game and what happens if you break them.”*

One member described how the CEO sets tone at the top through a combination of words and actions: *“Our CEO says, ‘Do the right thing.’ That mantra is repeated often. Normal human beings know how to do the right thing. Of course, once you say that, the CEO [then] has a responsibility to do it, and it can be painful. What [the CEO] says and lives filters down; it gets to everyone else ... It has a multiplier effect on the company ... You don’t get a day off. You can’t go the other way even once, or you lose it all.”*

CEOs interviewed for a 2004 issue of *InSights* were divided on the role the audit committee should play in helping to set the tone at the top: “Some CEOs see the audit committee as an essential partner in setting the tone at the top. Others believe the audit committee either has no specific role to play, or is simply too constrained by lack of time to play a meaningful part.”¹⁰

Members agreed that the audit committee cannot drive tone at the top. One member said, *“If there are culture issues within an organization, you need [leadership] from the CEO. If you make it an audit committee issue, it becomes a compliance issue, when it’s really a cultural issue. Be careful what the audit committee does and how it is involved. The audit committee has a supporting role.”*

Members described the following ways in which the audit committee can play that supportive role:

- **Undertake regular site visits.** *“We do it routinely.”*
- **Support the CEO’s direct reports.** *“The audit chair spends time with the direct reports of the CEO, especially in finance, because tone at the top is really important.”*

⁹ The Oxford University Press’s *Dictionary of Psychology* (2001) defines semantic satiation as “a peculiar sense of loss of meaning that occurs when a word is recited slowly 15 or 20 times in succession.”

¹⁰ Tapestry Networks and Ernst & Young, “The CEO perspective on the audit committee,” *InSights*, March 2, 2004, 2. Available at http://www.tapestrynetworks.com/documents/Tapestry_EY_ACLN_Mar04_InSights.pdf.

- **Be accessible to finance and internal audit staff.** *“I meet with the internal audit group and financial group ... to support their work and provide them with access to me.”*
- **Review employee survey data.** *“You can find out if employees feel there is a culture of compliance and can speak up without fear of retribution.”*
- **Provide guidance to the CEO.** *“At one point, my CEO came in and expressed displeasure with the length of audit committee meetings and the level of detail we were going into on some issues ... It was a strange interaction with the CEO. We pushed back, and the CEO apologized later, as it was inappropriate.”*

Conclusion

The relationship between the audit chair and the CEO is one of the most important yet most unexplored relationships in corporate governance. The CEO sets the tone at the top of the company that enables the audit committee to do its job and protect shareholders’ interests. The audit committee provides the CEO (and, ultimately, the shareholders) with assurance about critical financial information and with oversight of enterprise-wide risk; it also monitors the impact of tone at the top on compliance and ethics in the company.

The foundation of the relationship is mutual trust and respect, reinforced by regular, candid, and responsive two-way communication. There is also an opportunity for audit chairs to take the relationship further by defining and offering a clear value proposition to their CEO, but few audit chairs seem to have had an explicit discussion with their CEO regarding their mutual expectations. Without such a conversation, each may make assumptions about what the other wants or needs, and both may end up less than satisfied.

About this document

The Audit Committee Network is a group of audit committee chairs drawn from leading North American companies committed to improving the performance of audit committees and enhancing trust in financial markets. The network is convened by Ernst & Young and orchestrated by Tapestry Networks to access emerging best practices and share insights into issues that dominate the new audit committee environment.

ViewPoints is produced by Tapestry Networks to stimulate timely, substantive board discussions about the choices confronting audit committee members, management, and their advisers as they endeavor to fulfill their respective responsibilities to the investing public. The ultimate value of *ViewPoints* lies in its power to help all constituencies develop their own informed points of view on these important issues. Anyone who receives *ViewPoints* may share it with those in their own network. The more board members, management, and advisers who become systematically engaged in this dialogue, the more value will be created for all.

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Appendix: Consequences of the credit crisis

During another session on June 10, 2008, members discussed the consequences of the credit crisis, which continues to maintain a tight grip on U.S. public companies. One member noted, *“We’re still in crisis mode, and it’s too early to step back and learn from what’s happened. Perhaps 80% of the frenetic bit is done. There has been a move to ugly markets and recession – and it will be every bit as bad [as what we’ve just experienced].”* During the discussion, members focused on current challenges facing audit committees and on two longer-term concerns.

Current challenges for audit committees

Members cite valuation issues, exposures in company investments, Section 302 certification, and litigation risk as challenges their audit committees are currently facing, regardless of their industry.

- **Valuation issues.** Determining the fair value of financial assets and liabilities has been a particular focus for audit committees since the start of the credit crisis. Audit firms have issued guidance on how existing U.S. Generally Accepted Accounting Principles apply in this regard, as has the American Institute of Certified Public Accountants.¹¹ Financial Accounting Standard No. 157 (Fair Value Measurements), the new mark-to-market standard, has been a considerable source of concern: *“With mark-to-market, what do you do when there is no market? ... These are treacherous times.”* Another member stated, *“Fair values scare me to death. Last July, [one of my companies] did its annual planning. Three weeks later, the forecast was 100% different.”*
- **Exposures in company investments.** As the credit crisis has unfolded, audit committees have taken a hard look at the potential exposures represented by company investments. Even firms with seemingly conservative financial policies have found some AAA-rated securities have become illiquid. External auditors are advising audit committees to ask for assurance from financial staff and internal and external auditors that all exposures have been identified and quantified. Two specific concerns members raised were pension funds and counterparty risk. One member said, *“We still haven’t seen the ripple in the pension funds.”* The situation at Bear Stearns has brought counterparty risk concerns to the fore. One member asked, *“Do you think your companies know where their counterparty risks are?”* Another member responded, *“In terms of first order of effects, yes. You know who the first [is], but not the second or the third. They are very difficult to analyze and understand.”*
- **Section 302 certifications.** Section 302 of the Sarbanes-Oxley Act requires the most senior officer or officers of the company to certify their evaluation of the financial statements. Members reflected upon the increased risk this entails, given current market volatility. One asked, *“What advice do you give a CEO regarding signing the books?”*
- **Litigation risk.** Lawyers are reporting that the number of suits filed relating to the subprime crisis has risen dramatically, and they expect the trend to continue. Members acknowledged this trend at

¹¹ See American Institute of Certified Public Accountants, *Accounting for Underwriting and Loan Commitments* (New York: American Institute of Certified Public Accountants, 2007). Available at http://www.aicpa.org/caq/download/WP_Accounting_for_Underwriting_and_Loan_Commitments.pdf.

the session. Jamie Wareham, global chair of litigation at the leading international law firm Paul Hastings, told ACLN members in February that “the subprime meltdown could represent trillion-dollar losses.”¹² Attending a Southeast Audit Committee Network meeting in May, J. Kelley, the head of the Corporate Practice Group at the law firm King & Spalding, stated, “Volatility typically equals more cases, and the increased volatility we’re seeing means things will step up.”¹³ Audit committees will need to continue to work closely with their general counsel and legal advisers to assess the need to reserve for and disclose these new litigation risks.

Concerns for audit committees going forward

Members noted two concerns for audit committees going forward: the future of earnings guidance and the importance of enhancing risk management processes and monitoring risk appetite.

- **The future of earnings guidance.** Members discussed both the difficulty of providing accurate earnings guidance to the marketplace during a time of such volatility and the potential for litigation if company-issued guidance isn’t correct. Several members mentioned that some large public companies are considering limiting or even eliminating the provision of earnings guidance. The wisdom of providing guidance is also being questioned in governance circles. In June 2007, for example, the Aspen Institute’s Corporate Values Strategy Group (CVSG) proposed that companies and investors should “avoid both the provision of, and response to, estimates of quarterly earnings and other overly short-term financial guidance.”¹⁴ One member said, “*The conversation should be on the table.*”
- **Enhancing risk management.** The twin issues of risk management and risk appetite – which have both been blamed for the credit crisis – were discussed as ongoing challenges for all public companies, not just those in financial services. One member, commenting on the media coverage, said: “*[Risk management systems] weren’t adequate ... there were risks that weren’t expected.*” The credit crisis has stimulated interest in improving risk management, although skepticism about the effectiveness of enterprise risk management (ERM) programs may be hindering those efforts. ACLN members agreed there is significant work to be done: “*People feel more comfortable than they should.*” Whatever doubts they have regarding ERM, and despite the lack of good role models for risk management, members are convinced that audit committees will need to review their companies’ processes and management’s appetite for risk in order to avoid further financial dislocation in the future.

¹² Audit Committee Leadership Network, “Litigation risk and the audit committee,” *ViewPoints*, March 14, 2008, 3. Available at http://www.tapestrynetworks.com/documents/Tapestry_EY_ACLN_Mar08_View19.pdf.

¹³ Southeast Audit Committee Network, “Litigation risk and the audit committee,” *VantagePoint*, June 2, 2008, 3. Available at http://www.tapestrynetworks.com/documents/Tapestry_EY_SE_ACN_Jun08.pdf.

¹⁴ The Aspen Institute, *Long-Term Value Creation: Guiding Principles for Corporations and Investors* (New York: The Aspen Institute, 2007), 3. Available at <http://www.aspeninstitute.org/atf/cf/%7BDEB6F227-659B-4EC8-8F84-8DF23CA704F5%7D/FinalPrinciples.pdf>.