

Audit committee leadership

Managing the responsibilities of the audit committee is an evolving challenge for today's audit chairs. Effective committee leadership is more important than ever, especially as proponents of governance reform continue to push for increased audit committee responsibilities.

Corporate scandals have accentuated the importance of strong audit committee leadership. As one member noted, *"In all the recent failings, you can usually link these weaknesses to leadership competencies and traits."* Audit chairs are thus faced with both a growing scope of work and heightened responsibility to ensure their committees discharge their duties well.

Executive Summary

On 5 February 2021, members of the European Audit Committee Network (EACLN) met virtually for a members-only discussion of audit committee leadership.¹

For meeting participants, see Appendix 1 (page 9). For a list of discussion questions, see Appendix 2 (page 10).

- **Preparing for and leading a committee meeting** (page 2)

Audit chairs dedicate a significant amount of time before meetings to prepare, often by discussing the agenda, premeeting materials, and presentations with management, other directors, and the external auditor. Many members use these conversations to keep meeting materials concise and to highlight priority issues for committee discussion.

- **Maintaining a high-performing audit committee** (page 4)

Audit chairs discussed the challenges of building an effective audit committee, delegating responsibility to members based on expertise, and engaging the entire committee, especially when some directors are less vocal. Audit chairs also talked in depth about the growing importance of education sessions, not only for new members, but for the entire committee as the corporate governance landscape continues to rapidly evolve.

- **Defining the role and scope of the audit committee** (page 6)

As the oversight responsibilities of audit committees continue to grow, sharing some of those responsibilities with other committees and coordinating who is overseeing what becomes an increasingly complex challenge. Members discussed their practices around assigning oversight responsibilities and collaborating with other committees.

Preparing for and leading a committee meeting

Members described a wide range of practices around preparing for meetings, but a point of near complete agreement was that effective meetings require rigorous preparation. Working through the material ahead of a meeting not only allows audit chairs to better understand management's narrative, but also to think beyond management's presentation in order to ask better questions. A major reason for all this advance work, one member noted, is *"to avoid getting sucked into what's on the pages and miss what's not on the page."*

Prioritizing discussion over presentations in a meeting

Audit chairs agreed that a committee meeting is about discussion rather than presentation. Managing the time requires setting clear expectations. One member said, *"Before the meeting, I have a one-hour call with all the participants from management. We go through the agenda, and I ask them, 'What are the key messages you want to get across?' Then I tell them, 'If you have a 20- to 30-minute slot, you have to get the main ideas across in five minutes; then the rest of the time is for discussion.'" Another member noted, "You have to work hard with presenters on what is core." Several others concurred, with one observing, "You need a well-structured conclusion and a core presentation which aligns with the allocated time."*

Management is not alone in bearing responsibility here. *"The chair has a role as well,"* a member pointed out. *"You should have Q&A that is directed by what you as chair have identified as key topics or questions."* One audit chair described sending an email to the rest of the committee, directing attention to certain topics and specific pages in the meeting materials. Another said, *"I meet with all the presenters the day before the audit committee meeting. I spend six to seven hours with the external auditor, the CFO, etc. I say to them, 'This won't need so much detail,' or 'This, you need to explain more.' When you say management doesn't use the time properly, it's for the chair to make sure they do."* One member wryly noted, referring to management, *"We are good readers, so don't use slides, just talk to us."*

Working with management on meeting materials

To maximize time for discussing complex and controversial issues, members emphasized the importance of keeping meeting materials concise and tightly focused on what is most important for the committee to know. *"But this can be a challenge,"* one member pointed out. *"In the meeting, people can hide behind stuff you have already read."* Materials to be read in advance can often fail to highlight the key issues. As long as all committee members have read those materials, presentations can be minimized or eliminated entirely. Ultimately, as one audit chair put it, *"If we trust the people behind the papers, we don't need them. We would rather spend the time bringing people into the room."* But another asked, *"Do you assume everyone has read the material?"* One member said answering that question is an important aspect of setting the agenda. *"Everything is preread,"* a member said, regarding how she ran her committee meetings.

Members often work with management on materials, usually before papers go out to the rest of the committee, in order to ensure the right focus and level of detail. This forces management to distill the key messages. *"It's about focus ... We don't want to see more than*

15 pages of charts. The technical verbiage is otherwise sometimes impenetrable,” said one audit chair. Another said, *“When materials come in, I read everything ASAP. I can see what issues are coming and if they can address them. I note if some are weaker, and I reach out to the CFO or others who prepared materials, like the internal auditor. I tell them what to spend time on.”* Others had reservations about that approach: *“I have my doubts about bringing issues ahead” ... “I believe we need to challenge management. I won’t be able to challenge management if they are prepared.”*

Holding private sessions

Private sessions with key individuals or groups, such as the external auditor, the legal team, and financial and accounting executives, can streamline a meeting. These sessions also provide an opportunity for candid conversations and relationship building. They can be critical in identifying areas where the committee needs to probe and challenge. One member said, *“Before I see the CFO, I interact with the external auditor so I can challenge the CFO on things he would like us to go swiftly through which are worth investigating further. I do the same with the head of internal audit, the general counsel, and the head of compliance.”*

Members discussed a variety of practices around private sessions. The timing, number, and content ranged greatly across the audit chairs in attendance. Some reported private sessions conducted by the chair alone, while others expected the rest of the committee and even the CEO to be present.

Members described using private sessions to discuss a variety of topics. Some audit chairs use these sessions to refine agendas, coach management, or surface key topics. One member said, *“Real-time time allocation happens at private sessions at the beginning of the meeting.”* Other audit chairs have described private sessions as almost dress rehearsals for the meeting. But another member said, *“I don’t do a full dry-run—that would be one step too much.”*

Managing guest attendance at meetings

Managing the number of participants and meeting guests is critical, members said. *“It’s a balancing act,”* one commented, between the need to hear from a range of those in management and the fact that a large number of participants can slow down the agenda. *“With 20 people around the table, meetings do not work well,”* one audit chair said. Others described limiting those in attendance to the CEO, CFO, general counsel, and internal auditor.

Some members pointed out that senior managers in the ranks below the CFO are sometimes better able to answer detailed questions. Working with a range of executives can also surface potential problems. *“One of the most common reasons that problems do not become visible is because we always hear from the same people. I can tell you stories where if the board would have talked to one level below the CFO, they would have avoided some disasters,”* said one.

Indeed, many members approve of hearing from the next level down, provided the executives are well prepared. One member said, *“I love letting the next generation of talent shine through, and I like to see how they cope and handle coaching.”* Another member noted, *“These presentations are an opportunity to make someone better known to the committee, especially around succession planning.”* This member added that in some instances, hearing a

presentation *“has helped me get rid of someone I thought was very bad.”* Some do not support this practice, however: *“We are not a training ground. We want to see a great presentation, not provide feedback. Some CFOs no longer say anything themselves, but I want to start with the CFO addressing important topics. They don’t like it—they would rather put their controller, their [Sarbanes-Oxley] guy, etc., up front. However, in the first half-hour, you should get a good overview from the CFO. I want to feel like he’s on top of all the topics.”*

Engaging with the external auditor

Several members discussed the benefits of speaking with their respective external auditors before meeting with the CFO in preparation for audit committee meetings. One member noted, *“I get the full picture of where I should dig during the meeting with management.”* Others agreed on the importance of input from the external auditors, both before and during committee meetings. One audit chair described his practice: *“I call on our auditors. They have a separate time slot on the agenda, but in practice, as issues are dealt with, I will bring them in and get their views, so by the time we get to the external audit item on the agenda, their items have largely been addressed. It is important from a governance perspective to establish their views and give them a chance to comment.”*

It can take time for auditors to feel comfortable offering their input at audit meetings. *“You have to train your auditors,”* one member stated. *“A big part of this is the meeting I have before the audit committee meeting, where I ask them, ‘What is being done on this issue? What is happening in the industry?’ In the beginning, they were not at ease. They were worried about telling me what I hadn’t yet heard from management. Having a more open discussion takes years. I’m still pushing, but it’s improving.”*

Marie-Laure Delarue, EY’s global assurance vice chair, emphasized to members the importance of building a relationship of trust with the external auditor. Building that trust requires time, and Ms. Delarue agreed that frequent private sessions with the external auditor can be an effective way to build that relationship. In addition, she emphasized engaging not only with the lead audit partner but also other key partners and more junior members of the audit team. *“Communicate your expectations directly to the entire audit team, rather than just through the lead partner... Help us engage our young talents,”* Ms. Delarue said. *“It makes a huge difference.”*

Maintaining a high-performing audit committee

During the February meeting, members talked at length about the challenges of building an effective audit committee and finding a balance of expertise. One member noted, *“When people are being recruited to the board, their fit as potential audit committee members is not a high-priority consideration.”* Responding to the range of experience of board members,

another audit chair worried about getting too far ahead of the rest of the committee. *“It’s just discourteous if I just lead ... We need diverse audit committees. We need to be efficient, but we need to give everyone a chance.”* Diversity of experience, industry, and geography become important aspects in a board’s ability to effectively delegate its work. Otherwise, *“I feel like a single-lady orchestra at times,”* one member added.

Onboarding and training

Many members view onboarding and training new committee members as important audit chair responsibilities. *“I see it as part of committee leadership,”* one member said. On an audit committee, especially, the amount of work can be unnerving for new members. *“Some new members have no experience serving on an audit committee; they are overwhelmed by the workload,”* one audit chair noted. The need for training, however, is not limited to new members. *“Governance is evolving rapidly.”* With more regulations in the pipeline in many jurisdictions, members expressed the need for more training. *“We need to assess where real responsibility lies for training, compared to where things were a few years ago. Do we organize education sessions around specific issues and work with the auditors here?”*

Members agreed that there is typically no time for training during normal meetings. It must be organized outside the audit committee meeting. Some pointed out that the pandemic’s halt on travel had opened up time. *“We can use that time to have a virtual-dinner deep dive.”*

Some members pushed back on the notion that bringing new members up to speed is an audit chair responsibility: *“I don’t feel responsible for new member training. My role as chair is to make sure the audit committee is doing its work—preparing the meeting with CFO and being critical going through management’s material. The first requirement for the audit committee is making sure members can do the job.”*

Committee member engagement

One audit chair asked, *“How do you involve other members of the audit committee? Some are productive, some are more silent—they attend, but I don’t hear the sound of their voice.”* It falls on the chair to foster engagement: *“You have to give members feedback if they are not participating appropriately.”*

Several members discussed the practice of having all committee members submit their questions to management in advance of the meeting. In this way, audit committee members are incentivized to come prepared with questions. This method can also help ensure that all the committee’s questions get answered by management and the auditors during the allotted time for the presenters.

Multiple chairs recommended the practice of asking individual audit committee members to take leadership on particular issues as a way of encouraging active ownership and engagement. One member said, *“I ask individual members to be the point person on certain issues so I get a diversity of views.”*

Defining the role and scope of the audit committee

Part of managing an audit committee's agenda is determining the scope of its responsibilities. Many audit committees are now tasked with oversight of risks that include cybersecurity, major technology implementation, and environmental, social, and governance (ESG) matters. While audit chairs acknowledge that these added responsibilities make sense from a governance perspective, they report that the added responsibilities can test the capacity of a committee. In response, some boards are allocating oversight of certain risks to other committees. During premeeting calls, members expressed interest in discussing how peers coordinate agendas with other committees. For example, one asked, *"When there's both a finance committee and an audit committee, where are the boundaries and overlap?"*

Coordinating between the audit committee and other committees

Joint meetings and cross-committee membership are a common way to approach this challenge, a member said. *"It is important for the audit committee chair to be on the remuneration committee or vice versa."* But some pointed out that cross-committee membership may not be enough. *"Cross-representation is not the answer. They tend to get pulled into the other committee's agenda, rather than being devil's advocate for audit and asking, 'Am I getting what I want?'"*

Several members emphasized that the audit committee's scope should be updated regularly. One highlighted the *"need to keep realigning charters between committees because we have lots of dependence on other committees' work."* Transitions in committee leadership can provide an opportunity to revisit responsibilities. Changes in the operational or business context can lead to changes in committee responsibilities. One member recalled, *"After compliance expanded in scope following an investigation, we had a discussion about whether to have a separate compliance committee. I spoke up and said we should have a single audit and compliance committee—an internal signal that compliance was high on the agenda."*

Allocating risk oversight

Sharing oversight responsibilities with other committees can alleviate some of the pressure on the audit committee. Risk and audit committees often have overlapping members, and the distinctions in responsibilities can become unclear at times. In some cases, while the full board or another committee might own oversight of specific risks, such as cyber or operational risk, the audit committee retains responsibility for the overall risk management framework and for assuring that all risks are being addressed. This was the case for one member, who described their board's division of responsibilities for risk thus: *"The risk committee handles operational risk, while the audit committee handles overall risk, including compliance, legal, internal audit, and financial risk."* Another audit chair expanded on the division of responsibility: *"The risk committee chair proposed eliminating duplication between the risk and audit committees. In so doing, the risk chair returned to the audit committee sole responsibility for liquidity, tax, and internal audit risks. The risk committee gets a copy of the audit committee's meeting materials, so it knows what we're covering. We get an annual or semiannual report from the risk committee so we can understand the key enterprise risks they're handling."*

Ensuring oversight of new and emerging risks

When new risks or issues rise to the board's attention, how are these assigned across committees? While some members welcome the added oversight responsibilities that fall under the audit committees' purview, others are wary of having the committee take on too much and would prefer new responsibilities to go to the full board. Members worry that too many new issues landing on the audit committee could undermine the committee's core mission of overseeing financial reporting: *"We can't take everything on for the board. We need to make sure that accounting issues are adequately covered."*

During premeeting calls, several members pointed to ESG as a relatively new risk area where oversight responsibility commonly requires further clarification. One member described a board's division of labor for sustainability oversight: *"We had a joint meeting between the audit committee and the sustainability committee, where we had a discussion around the interrelationship between the sustainability committee, which sets targets, and the audit committee, which focuses on integrated disclosures. The reporting is more with the audit committee; the work program is more for the sustainability committee."* Another described a similar dynamic: *"ESG fits with the audit committee in a way. Especially if [International Financial Reporting Standards] take it on, then there could be a good connection because it will go to the annual report, and that's an audit committee skill set. But in those companies, there's also a sustainability committee, so does this fit with the sustainability committee and its work on carbon pricing?"*

Conclusion

While nearly every audit committee has the same oversight responsibilities for financial reporting, no two committees are identical. As a result, members described a wide array of committee leadership practices. Yet many commonalities emerged during the EACLN discussion: effective meetings begin with rigorous preparation, and ongoing communications with management and the external auditors ensure that the board and its committees function well, both independently and in collaboration with each other.

About this document

The European Audit Committee Leadership Network is a group of audit committee chairs drawn from leading European companies committed to improving the performance of audit committees and enhancing trust in financial markets. The network is organized and led by Tapestry Networks with the support of EY as part of its continuing commitment to board effectiveness and good governance.

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. Those who receive *ViewPoints* are encouraged to share it with others in their own networks. The more board members, members of management, and advisers who become systematically engaged in this dialogue, the more value will be created for all.

The perspectives presented in this document are the sole responsibility of Tapestry Networks and do not necessarily reflect the views of network members or participants, their affiliated organizations, or EY. Please consult your counselors for specific advice. EY refers to the global organization and may refer to one or more of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Tapestry Networks and EY are independently owned and controlled organizations. This material is prepared and copyrighted by Tapestry Networks with all rights reserved. It may be reproduced and redistributed, but only in its entirety, including all copyright and trademark legends. Tapestry Networks and the associated logos are trademarks of Tapestry Networks, Inc., and EY and the associated logos are trademarks of EYGM Ltd.

Appendix 1: Participants

The following EACLN members participated in part or all of the meeting:

- Jeremy Anderson, UBS
- Julie Brown, Roche
- Aldo Cardoso, Bureau Veritas
- Carolyn Dittmeier, Assicurazioni Generali
- Liz Doherty, Novartis and Philips
- Eric Elzvik, Ericsson
- Renato Fassbind, Nestlé and Swiss Re
- Byron Grote, Tesco, Akzo Nobel, and Anglo American
- Margarete Haase, ING
- Liz Hewitt, National Grid
- René Hooft Graafland, Ahold Delhaize
- Dagmar Kollmann, Deutsche Telekom
- Pilar Lopez, Inditex
- Benoît Maes, Bouygues
- Hanne de Mora, Volvo Group
- Stephen Pearce, BAE Systems
- Ana de Pro Gonzalo, STMicroelectronics
- Nathalie Rachou, Veolia
- Jon Erik Reinhardsen, Telenor Group
- John Rishton, Unilever
- Mariella Röhm-Kottmann, Zalando
- Sarah Russell, Nordea Bank
- Guylaine Saucier, Wendel
- Erhard Schipporeit, RWE
- Carla Smits-Nusteling, Nokia and ASML Holding
- Maximilian Zimmerer, Munich Re

The EY organization was represented in all or part of the meeting by the following:

- Marie-Laure Delarue, EY Global Vice Chair, Assurance
- Jean-Yves Jégourel, EY Global Assurance Vice Chair, Professional Practice
- Julie Teigland, EY EMEA Area Managing Partner



Appendix 2: Discussion questions for audit committees

- ? What are some practices for helping management present materials to the committee more effectively?
- ? What is the right balance between hearing from the CFO and other c-suite executives and hearing from the next level of executives?
- ? What are some effective practices for drawing out the external audit partners during audit committee meetings?
- ? What are effective strategies for negotiating sensible boundaries between the responsibilities of the audit committee, other committees, and the full board?
- ? How do you determine whether and when to create a new committee or to assign oversight of a particular issue or risk to a different committee?



Endnotes

¹ *Viewpoints* reflects the network's use of a modified version of the Chatham House Rule whereby comments are not attributed to individuals or corporations. Quotations in italics are drawn directly from conversations with network members in connection with the meeting.