

AUDIT COMMITTEES

A GUIDE TO GOOD PRACTICE

Third Edition

A joint publication by the Auditing and Assurance Standards Board,
Australian Institute of Company Directors and
The Institute of Internal Auditors–Australia



Australian Government
Auditing and Assurance Standards Board

AUSTRALIAN INSTITUTE
of COMPANY DIRECTORS



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Chapter 1

Introduction

An audit committee is a committee of a board of directors (the board), operating under delegation of authority from the board. Its objectives are clearly defined and documented in its charter and its efficiency and effectiveness are measured by reference to its objectives.

An independent audit committee is a fundamental component of good corporate governance.¹

Typically, an audit committee:

1. focuses on issues relevant to the integrity of an entity's financial reporting;
2. oversees external audit, internal audit,² risk management, internal control and compliance; and
3. liaises with the board, internal auditors, external auditors³ and management.

Some entities establish one committee with the responsibility for all of these tasks, such as an audit and risk management committee. Larger entities may establish more than one committee, such as an audit committee, a risk and compliance committee, a health and safety committee and an environmental committee depending on the nature and extent of the entity's operations.

1 Principle 4: *Safeguard Integrity in Corporate Reporting*, Recommendation 4.1 of the 3rd edition of the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations*.

2 See glossary for definitions.

3 See glossary for definitions.

Who should use this guide?

This guide is primarily for directors and audit committees of Australian listed companies. Directors, boards of management and audit committees of not-for-profit, public sector,⁴ and other private sector entities, may also find this guide to be a useful reference.

There is no “one size fits all” good practice solution for audit committees. The nature of the business, the regulatory environment, ownership structure, legal requirements, and audit committee membership influence the objectives and activities of an audit committee. Smaller entities with limited resources might find it impractical to meet all of the practice solutions outlined in this guide. They may use this guide to assess the elements of good practice that are relevant for their financial reporting, corporate governance, risk management and internal control, and exercise them at the board or committee level.

Purpose of this guide

This guide provides a practical introduction to the role and responsibilities of an audit committee. It explains the context in which an audit committee typically operates and outlines good practice.

While the guide assists the board and audit committee members, it may also be helpful to risk and compliance managers, internal auditors, external auditors and senior management, as it explains the expectations and accountabilities between the audit committee and these other parties.

Clarifying the roles and responsibilities between the audit committee, risk and compliance managers and auditors (both internal and external) assists their communication, efficiency and effectiveness. Using this guide assists audit committees in assessing an entity’s external financial and other internal and external reporting requirements. It also assists in assessing the effectiveness of an entity’s risk management and internal control systems.

This third edition of the guide reflects developments in audit committee practice, legislation and guidance from regulatory bodies and in leading global board practices

⁴ Federal and state bodies should also consider their own specific guidance relating to the operation of their audit committees.

since the previous edition was published in 2012. It has been produced by the Auditing and Assurance Standards Board, the Australian Institute of Company Directors and The Institute of Internal Auditors–Australia.

The guide does not attempt to advise directors or members of audit committees about their legal duties. For a general discussion of directors' duties, refer to *Duties and Responsibilities of Directors and Officers*, 21st edition, by Professor Robert Baxt AO, published by the Australian Institute of Company Directors in 2016.

Recent developments regarding audit committees

Since the previous edition of this guide was published in 2012, some of the key developments in Australia include:

- January 2017 – The Institute of Internal Auditors Inc (IIA) issued a revised *International Professional Practices Framework* (IPPF). The IPPF has been adopted by The Institute of Internal Auditors–Australia (IIA–A) and was effective from 1 January 2017. The changes mainly affect the International Standards for the Professional Practice of Internal Auditing and have generally been made for clarification purposes.
- December 2016 – revised Australian Auditing Standards came into effect, some of which impact the operation of audit committees as they change the requirements in relation to an auditor reporting to the board. Examples include the Auditing Standard ASA 700 series, including the new ASA 701 *Communicating Key Audit Matters in the Independent Auditor's Report*, revised ASA 720 *The Auditor's Responsibility Relating to Other Information* and related consequential changes to other relevant auditing standards, such as ASA 260 *Communication with Those Charged with Governance* and ASA 570 *Going Concern*.
- August 2016 – The IIA issued *Supplemental Guidance: Applying the International Practices Framework as a Professional Services Firm* which provides some clarification about the services of internal auditing as distinct from external auditing.
- June 2015 – The Australian Securities and Investments Commission (ASIC) issued Information Sheet 203: *Impairment of non-financial assets: Materials for directors* explaining the responsibilities of a director in

connection with the testing of non-financial assets for impairment in the financial report of a company.

- December 2014 – ASIC re-issued Information Sheet 183: *Directors and financial reporting* covering the financial reporting responsibilities as a director.
- March 2014 – the ASX Corporate Governance Council⁵ released the 3rd edition of the *Corporate Governance Council Principles and Recommendations*. These revised guidelines came into effect from 1 July 2014 and broaden Principle 4 to encompass corporate reporting rather than just financial reporting.
- March 2014 – ASIC issued Information Sheet 196: *Audit quality – the role of directors and audit committees* (INFO 196) providing guidance to assist directors and audit committees in their role in supporting the quality of the external audit of the financial report.
- February 2014 – the International Auditing and Assurance Standards Board (IAASB) issued *A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality* which encourages all participants in the financial reporting supply chain, including audit committees, to challenge themselves to do more to increase audit quality in their particular environments.
- January 2014 – The Australian Prudential Regulatory Authority (APRA) revised *Prudential Standard CPS 510 Governance* from 1 January 2015 and the new *Prudential Standard CPS 220 Risk Management*. Revisions of these guides have since been issued and come into effect from 1 July 2017.

5 The ASX Corporate Governance Council was formed in August 2002 and brings together various business, shareholder and industry groups to enhance corporate governance practices in Australia. Its ongoing mission is to ensure that the principles-based framework it developed for corporate governance continues to be a practical guide for listed entities, their investors and the wider Australian community.