

AGB

**Effective
Committee
Series**

The Audit Committee

by Richard L. Staisloff



Table of Contents

Introduction: <i>Effective Committees</i>	1
Section 1: <i>Introduction to the Audit Committee</i>	4
Section 2: <i>Purpose of the Committee</i>	9
Section 3: <i>Committee Responsibilities</i>	11
Section 4: <i>Committee Composition</i>	27
Section 5: <i>Tips for Effective Audit Committees</i>	29
Section 6: <i>Pitfalls and Lessons</i>	31
Section 7: <i>Conclusion</i>	33
Appendix A: <i>Sample Audit Committee Charter</i>	34
References and Resources	38
About the Author	40

Effective Committees

This publication is part of an AGB series devoted to strengthening the role of key standing committees of governing boards. While there is no optimum committee system for institutions of higher education, certain principles, practices, and procedures prevail. The best practices outlined below support the objectives of board committees: focused effort, informed decision making, and self-management.

FOCUS THE WORK OF COMMITTEES

The work of boards should be grounded in the work of its committees. Working in tandem, committees enhance the purpose and advance the productivity of the full board.

1. Committee charters should clearly declare the governance purpose of each committee.
2. Committee work should be aligned with the institution's strategic vision, goals, and priorities.
3. Committees should translate their charges into annual goals and work plans that align with the board's governance responsibilities and the institution's strategic plan.
4. Committees should focus on monitoring the institution's strategic progress and the committee's accomplishments.
5. Committee meeting agendas should be concise, developed in consultation

with the committee chair and designated staff member, clearly state desired meeting outcomes, and they should be distributed—with appropriate supporting documents—well in advance.

6. Committee members should strike an appropriate balance between “too much” and “too little” information. They must guard against requesting overly detailed information to avoid becoming embroiled in administration or overburdening staff. At the same time, they need sufficient supporting materials to make sound recommendations and ensure adequate oversight.

FACILITATE INFORMED AND PARTICIPATORY DECISION MAKING

Committees are responsible for recommending decisions and actions to the full board. They should serve as models of good governance, where issues are debated and recommendations are framed openly, inclusively, and with full transparency.

1. Committees should deliberately include constituents whose voices have legitimate bearing on the topics under consideration.
2. Board members and constituents should have an active and reciprocal understanding of their respective roles and responsibilities within the institution’s governance structure.
3. Through committees, board members and the institution’s constituents should engage in a dialogue that demands facts and explores critical issues within the appropriate boundaries. Jointly and based on mutual trust, they should learn to ask the right questions that honor governance prerogatives and advance the institution’s strategic direction.
4. When making formal recommendations to the full board, committees should present conclusions that summarize relevant data and findings, including constituent voices and diverse perspectives.

ORGANIZE THE WORK OF COMMITTEES

While board bylaws often define the committee structure, the needs of each committee vary depending on the committee’s purpose and the institution’s changing circumstances. Within the division of labor between committees and the board, committees have responsibility for managing their own policies and practices.

Introduction to the Audit Committee

Colleges and universities and their related foundations have become subject to intensive scrutiny, not only by the public, the press, governmental agencies, and financial institutions but also by alumni, donors, faculty, and students. This scrutiny has, in turn, resulted in a new institutional focus on accountability, transparency, and enterprise risk management, as well as efficient and effective operations. Audit committees serve to ensure that these concerns are continually met through the preparation of accurate and timely financial statements; adequate internal control; compliance with laws, regulations and donor intent; and management of operating risks. In this way, the audit committee serves as the guardian of an institution's most valuable asset: its reputation.

THE EXTERNAL ENVIRONMENT

A review of the external environment confirms the necessity of focused, active board attention to accountability, transparency, and risk. At the federal level, the Internal Revenue Service continues to increase the required level of disclosure for nonprofit organizations through the release of the new Form 990. The passage of the Higher Education Opportunity Act of 2008 significantly increased compliance requirements on institutions, ranging from textbook prices to illegal file sharing. Finally, the provisions of the Sarbanes-Oxley Act continue to influence expectations of governance and oversight by boards. This scrutiny is also apparent at

the state level, with states' attorneys general launching investigations into higher education practices. A strong, well-functioning audit committee is a necessity if institutions and related foundations are to ensure that they are addressing these heightened requirements. (Throughout this publication, the term "institutions" refers to independent and public colleges and universities and their related foundations. Differences in requirements, practices, and other aspects of the audit committee's work are noted.)

THE INTERNAL ENVIRONMENT

While the full board has broad fiduciary responsibilities, the audit committee serves as the institution's first line of defense when considering financial reporting, internal control, compliance, and risk management. The audit committee, therefore, is an essential component for the board to meet its fiduciary role. As such, the board must give careful attention to committee membership and ongoing professional development in order to ensure that appropriate resources are invested in the committee.

"While the full board has broad fiduciary responsibilities, the audit committee serves as the institution's first line of defense when considering financial reporting, internal control, compliance, and risk management."

The 2011 AGB Survey of Higher Education Governance showed a dramatic shift over the past seven years in the number of boards reporting the creation of a separate audit committee. In the 2004 survey, audit committees appeared for the first time as one of the top 10 most common committees, with 39 percent of independent institutions and 23 percent of public institutions reporting a separate audit committee. By 2011, 65 percent of boards of independent institutions reported separate audit committees, compared to 45 percent of boards of public institutions. (See Exhibit 1.) Boards of foundations affiliated with public institutions showed a similar prevalence in the creation of separate audit committees. In a 2007 AGB study¹, 57 percent of foundation boards reported having a separate audit committee. By 2010, AGB data² showed 70 percent of foundation boards reported a separate audit committee, with the remaining 30 percent having a combined finance and audit committee.

1. *AGB Survey of Foundation Governance Practices and Changes Made Since 2002*. AGB, 2007.

2. *Policies, Practices and Composition of Institutionally Related Foundation Boards*. AGB, 2011.