Audit Point of view

Best practice makes perfect sense

Audit committee learnings from leading Canadian financial institutions

Of the financial crisis’ many ramifications for businesses, the rising complexity of the regulatory environment has without doubt been one of the most broadly impactful. Due to its inherent connection to the crisis itself, the financial services industry has been first and foremost in dealing with the fallout, as global regulators quickly began looking more closely at what financial institutions (FIs) were doing from a risk and operating perspective. With banks pushed, as a result, to consider business more and more through a risk lens, bank audit committees (ACs) have correspondingly expanded their oversight role to ensure the appropriate range of compliance processes are in place so the organization stays compliant without compromising its strategic business focus.

Learnings honed in the crucible

The point is, this environment has placed banks front and center when it comes to the evolution of the audit committee, with respect both to its expanding risk role and in dealing with the challenges a growing risk mandate creates around more traditional duties. FIs, of necessity, continuously review these issues and revise their approaches, at both the AC and board levels. Indeed, the ongoing strength of the Canadian banking system has accorded our FIs a distinct leadership role in this area.

With that in mind, some of the AC practices Canadian banks have been developing may be of interest to other organizations, although applicability will vary with specific company circumstances and industry. FI best practices include:

**AC and risk committee separation**

Although AC oversight of risk is increasing in many areas, FIs have found it’s important that organizations continue to look at risk differently than they do reporting matters. As such, many maintain clear differentiation between the roles. Some risks clearly come under the AC’s umbrella, and it can certainly be valuable to have joint AC/risk committee membership for some directors or have each chair monitor the other’s committee. However, the demands of each role are too many and too significant to roll into one.

**Focus on four control functions**

Finance, internal audit, risk and compliance are four key areas for FIs and should be top-of-mind when it comes to AC or risk committee oversight focus. Many banks now have each of these control functions conduct an annual internal self-assessment against a set of good governance and good process guidelines, addressing issues such as internal function succession planning. Regulators are interested in and supportive of such processes, so it’s critical for the AC to review those assessments and monitor overall governance around each function.

**Stakeholder communications**

With the stakes as high as they are, ACs understand the value of improving stakeholder communications. For example, ACs and regulators meet face-to-face more often to discuss a range of risk and regulatory issues and the processes needed to address them. The chair of the AC should also meet at least quarterly with the heads of each of the four key control functions mentioned above. It’s about expanding perspective, seeing things from an internal as well as an external point of view.
Limiting the number of board memberships for individuals

Active board members used to sit on as many as seven or eight boards, numbers which are no longer feasible. Some guidelines suggest only three should be the maximum. Directorship is simply more time consuming and demanding than in the past. It can be a full-time job keeping up with information and building the key relationships an effective board role requires—especially with multiple memberships. To make the time commitment workable and participation effective, the number of boards served on must be limited.

Maximize best practice resources

Banks, in particular, have proven highly interested in what other banks are doing in Canada and around the world. This increasingly collective approach, along with their focus on risk/compliance and a willingness to leverage the broad industry knowledge of their external auditors, has significantly enhanced the ability of leading financial institution audit committees to augment and fine-tune their best practices. Organizations of all types and in all sectors may find that taking a closer look at those practices can be a valuable exercise.

Contact us

Kristy Carscallen
Canadian Managing Partner, Audit
T: 416 777-7137
E: kcarscallen@kpmg.ca