KPMG

Audit Committee Institute

On the 2016 Audit Committee Agenda

Prioritising a heavy audit committee agenda is never easy, and 2016 will be particularly challenging given the level of global volatility and uncertainty – e.g. the geopolitical environment, commodity prices, interest rates, currency fluctuations, slowing growth in emerging markets – as well as technology advances disrupting established industries and business models. Drawing on insights from interactions with audit committees and business leaders over the past year, ten items have been flagged for audit committees to keep in mind as they consider and carry out their 2016 agendas:

Maintain control of the audit committee's agenda.

This number-one priority from last year holds true for 2016:

Overseeing the major risks on the audit committee's agenda in addition to its core responsibilities (financial reporting and auditor oversight) remains a challenge. Even in the absence of any new agenda items, the risks that many audit committees have had on their plates for some time – cyber and IT, supply chain and other operational risks, legal and regulatory compliance – have become more complex, as have the audit committee's core responsibilities. Keeping the committee's agenda focused and its eye on the ball – will require an agenda that is manageable (what risk oversight responsibilities are realistic?); a sharp focus on what's most important (starting with financial reporting and audit quality); allocating time for robust discussion while taking care of 'must do' compliance activities; maximising the value of internal audit (as the committee's 'eyes and ears'); and ensuring the committee has the right composition and leadership.

Monitor and scrutinise critical accounting estimates.

Fair values, impairments, and judgments of key assumptions underlying critical accounting estimates, together with loss contingencies and pension funding shortfalls should continue to be a major area of focus for the audit committee. Recognise that the company's greatest financial reporting risks are often in those areas where there is a range of possible outcomes and management has to make difficult judgments and estimates. Regulators globally continue to express concern about adverse inspection findings pertaining to critical accounting estimates. The message: quality financial reporting requires a disciplined, robust, and unbiased process to develop accounting judgments and estimates. To that end, understand management's framework, help ensure that management has appropriate controls in place, and ask for the external auditor's views.

Stay apprised of the audit reform initiatives.

The EU Audit Reforms – and the implications for auditor rotation, non-audit services and the role of the audit Committee – will become a reality. Also, new International Standards on Auditing (ISA) requirements will impact the reports your auditors provide. Companies Act 2014 introduces a requirement for the directors of a company over a particular size to either establish an audit committee or to explain in the directors' report why they have not decided to establish an audit committee. Companies Act 2014 also presents choices for directors in terms of re-registering their company as a Designated Activity Company ("DAC") or a Private Company Limited by shares ("LTD"). A DAC more closely resembles a Limited company prior to the introduction of Companies Act 2014. Stay apprised of these initiatives and consider how they will impact the audit process and the audit committee's oversight.

Reinforce audit quality and set clear expectations for the external auditor.

Audit quality is enhanced by a fully engaged audit committee. Set the tone and clear expectations for the external auditor, and monitor auditor performance through frequent, quality communications and a robust performance assessment. Do the audit committee, management, and the external auditor have a clear understanding of audit quality and how it can be improved (or at least maintained)? Remember that audit quality is a team effort, requiring the commitment and engagement of everyone in the process - the auditor, audit committee, and management.

Consider how the company's disclosures can better tell the company's story – and that of the audit committee.

Think about providing a fuller picture not only of the company's recent performance, but also where it is headed, the key risks it faces and how those risks are both mitigated and factored into the group's viability statement. In addition to traditional financial metrics, can the company provide greater insight into the drivers of long-term growth, such as customer satisfaction, talent, or innovation? Many companies are experimenting with new ways to present clearer and more concise annual reports. Also, consider ways to enhance the audit committee's disclosures to provide greater insight into how the audit committee carries out its oversight responsibilities – focusing on what the committee did, what it concluded and how and why it came to those conclusions.

Maintain a sharp focus on finance leadership and bench strength.

Quality financial reporting starts with the CFO and finance department. Given the critical role the CFO plays in maintaining financial reporting quality, it is essential that the company has succession plans in place not only for the CFO, but for other key finance executives – the controller, chief accountant and treasurer (and perhaps the chief compliance and chief risk officers). How does the audit committee assess the finance department's talent pipeline? Do they have the training and resources they need to succeed? How are they incentivised to stay focused on the company's long-term performance?

Spend more time outside the boardroom.

Recognise that effectiveness inside the boardroom hinges on spending quality time outside of the boardroom – visiting company facilities, interacting with employees and customers, and hearing outside perspectives – to understand the tone, culture, and rhythm of the organisation.

Assess the company's readiness for country-by-country tax reporting.

The obligation to report country-by-country tax information to all jurisdictions is on the immediate horizon – with significant implications for tax compliance and reporting functions, transfer pricing policies, tax audits and controversies, and reputational risk for multinational companies. Under the OECD's Base Erosion and Profit Shifting (BEPS) project, multinationals with more than €750 million in revenue will be required to provide, in a single country-by-country (CbyC) report, detailed information about every jurisdiction in which they operate. The first CbyC reports will relate to fiscal years beginning on or after 1 January 2016, with the report due one year later. Audit committees of multinationals will want to assess their company's readiness. What systems and process changes will be needed to comply with the requirements? Have they assessed their transfer pricing strategies and identified those that are likely to be challenged? Do they have an effective communications plan to explain and interpret the CbyC data?

Assess the company's readiness for the new revenue recognition standard.

The IASB has finalised the deferral of the effective date of the new revenue standard by one year – until 1 January 2018 for calendar year-end companies. The new standard, which will change the way many companies recognise revenue from customer contracts, will have a significant impact across the company – from systems, data, and accounting processes, to controls and business contracting processes. Companies should use the additional transition time to finalise implementation plans, identify areas that require close attention, and implement the necessary changes to processes, systems, and controls.

Be prepared for data and analytical procedures.

Audits are changing significantly. The core goals remain, but audit tools, execution and results are being transformed and expanded by new capabilities in data and analytics (D&A). This is more than a trend. This is the way audits will be conducted by virtually all the major audit firms, and it is critical that audit committees and auditors begin working together now so audit committees understand where the process is heading, what the broad benefits are and how to work effectively with management to enable a smooth and effective shift within their organisations.

Also see KPMG's "On the 2016 Audit Committee Agenda" at kpmg.ie/aci.

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