Introduction

- Recent financial crises have again placed focus on the governance of organisations and public sector organisations are not immune

- Greater need for improving corporate governance and increased expectations placed on audit committees’ effectiveness in private sector

- Relatively little consideration has been given to the issue of audit committees’ effectiveness in the public sector

- Historically, focus has been on the transfer of commercial models of governance to public sector organisations
Purpose of this presentation

- To explore elements of risk management and effectiveness in the context of public sector audit committees

- To identify some of the advantages and disadvantages, problems and solutions associated with public sector audit committees
Audit Committees in the Public Sector

- Audit Committees in the private sector
  - High profile corporate collapses in Australia
  - Ramsay Report (2001) recommendations: for all public listed companies on the Australian Stock Exchange (ASX) to have an audit committee
  - ASX Corporate Governance Council (2003)’s Principles of Good Corporate Governance and Best Practice: the board of listed companies have an audit committee
  - CLERP 9 (2004)’s requirements: the top 500 listed companies on the ASX to have an audit committee
Audit Committees in the Public Sector

- public sector agencies generally established via different legal arrangements

- less commonality between separate jurisdictions than is the case in the private sector (profit leveller and wealth creation)

- the establishment of an audit committee and/or an internal audit function may depend on the specific legislation and/or practice in a jurisdiction

- no mandated requirement for agencies to establish an audit committee in any legislation BUT received wisdom of having one
Audit Committees in the Public Sector

• Core Responsibilities: to oversee the effectiveness of:
  – risk management framework
  – monitoring the internal control environment and the reports of internal auditor
  – legislative and regulatory compliance
  – external audit coordinating and
  – integrity of financial reporting
Audit Committees in the Public Sector

• Are audit committees appropriate in the public sector?

Yes – a governance mandate which:

– agencies need to be accountable to tax payers
– it may be an integral part of an organisation's corporate governance mechanism
– ensures appropriate systems and processes in place
– ensures the integrity of financial information
– identifies, evaluates and manages risks in the public sector
– manages risks related to government agencies restructure
Audit Committees in the Public Sector

- Benefits of having audit committees in the public sector
  - to focus on financial and compliance issues
  - to enable management to make better decisions
  - to help agencies to use resources in a more efficient way
  - to strengthen the internal audit function
  - to reinforce agencies’ accountability
Audit Committee Composition in the Public Sector

- The increased need for audit committees to be comprised solely of independent directors after the Global Financial Crisis

- At least one of the committee members should have some degree of financial knowledge (compare with private sector committees)

- Members’ combined experience, skills, and personal qualities may be different from those in private sector in that a broader understanding of objectives may be necessary
Audit Committee Composition in the Public Sector

- Audit committee members in the public sector should particularly possess such attributes as:
  - ability to maintain independence and objectivity in the context of a politically driven environment
  - have skills such that they can advise the governing body or chief executive of matters need further attention within that political framework
  - sound knowledge of the government financial and performance reporting framework
Audit Committee Composition in the Public Sector

• Audit committee members in the public sector should particularly possess such attributes as:

  – familiarity with the public sector’s legislation, policies, culture and values
  – a good understanding of the roles of internal audit and the Auditor General
  – a good understanding of their responsibilities with regard to corruption reporting and broad concepts of performance and performance reporting
  – an appreciation of the political framework
Audit Committee Effectiveness in the Public Sector

- Audit committee effectiveness has normally been examined in terms of:
  - the extent of independence
  - frequency of audit committee meetings and member attendance
  - the extent of interaction between the audit committee and internal audit function
  - relationships with Board Directors, CEO, Chief Finance Officer and External Auditors
Challenges

1. To find appropriate people who are independent of the organisation with sufficient knowledge of the organisation, government financial reporting framework and an ability to identify, evaluate and resolve the risks

2. It may be a challenge for the chairperson of the audit committee in a government department if she / he cannot get full support of the chief executive

3. Audit committee members in the public sector need to consider both the positive and negative impact of continuing use of external contractors to perform internal audit work
Challenges

4. Budgetary and economic conditions may bring different risks for management and the Audit Committee in the public sector to consider.

5. There is a need to improve audit committee members’ understanding of the nature of risk within their organisations - reputation, compliance.

6. It is essential for the chairperson of the audit committee to have regular contact with the board chairperson or the chief executive.
Challenges

7. There may be an expectation gap between the audit committee and management:

The audit committee’s expectation from management:
– to have a positive attitude to the findings and recommendation
– to have a constructive approach to interacting with the audit committee
– to be supportive in identifying potential areas of risk
– to keep the audit committee informed of the agency’s strategic plans, any investigations or any probity issues
Challenges

- The management’s expectation from the audit committee:
  - to communicate about its activities and reports
  - to be able to identify high risk areas; to see the wood for the trees
  - to focus on the main areas of risk and business improvement opportunities
  - to make recommendations by considering the cost and reality to implementation
  - to create a continuous improvement culture
Conclusion

Audit committee can be a very important part of good corporate governance mechanism in the public sector, to improve its effectiveness, there need:

• to have a supportive and positive culture from the top
• to maintain members’ independence and ensure recommendations are accepted
• to increase members’ understanding of the nature of the risks within their organisation
• BUT – an audit committee is not always required, necessary or even appropriate in all situations.
Questions?