New audit committee member/director onboarding

KPMG's Audit Committee Institute

For any new director—particularly when joining the audit committee (AC)—a learning curve comes with the territory. Just how steep that learning curve is, however, and how quickly a new director is able to contribute meaningfully to the work of the board and its committees, can hinge directly on the quality of the onboarding process.

Understanding the business—its operations, strategies, risks, and management team—as well as the responsibilities and culture of the board and its committees takes time. But a structured onboarding process—including essential information and briefing materials, quality discussions with key people, and a "road map" for getting up to speed—can greatly accelerate a new director's integration and contribution to the board's work.

For new AC members, onboarding presents an added layer of complexity, given the intricacy and scope of the financial reporting/accounting and legal/regulatory compliance issues on the AC's plate.

We offer the following framework for new AC members—and the management and audit professionals supporting them—to consider as they develop an onboarding process, including:

- Suggested reading for the new AC member, such as corporate documents and other briefing materials
- An initial orientation session
- Follow-up one-on-one meetings with key people in the organization to develop a deeper understanding of the business, its key governance processes, and its leaders

Formal orientation programs for new directors are fairly common, but these programs—without more—may be inadequate to get the new director up to speed and able to contribute to the work of the board early on. Moreover, the onboarding needs for new directors will vary from director to director, depending on a number of factors, including the director's background and experience, and the role the director is expected to play on the board and board committees. As a result, a new director should be prepared to take responsibility for his or her onboarding plan—working with management and others to determine how best to get up to speed and build a strong foundation for informed oversight.

Suggested background reading materials

A new AC member will want to review a number of corporate documents and background materials early on, including:

Information about the company, with a financial reporting emphasis, including

- Financial statement reports (Form 10-Q and 10-K) for the previous two years, as well as proxy statements and Form 8-Ks
- Earnings releases and materials used for analysts' calls for the past year or two
- Recent comment letters from the Securities and Exchange Commission (SEC) and the company's responses
- The most recent "board book"
- Bios of senior financial management (including internal audit (IA))
- The company's strategic plan and latest risk reports
- Reports from management's disclosure committee (if applicable)
- Recent contingent liability (litigation) reports

- Recent analyst reports on the company and the industry, as well as industry/competitor information prepared by management
- Company's Code of Conduct (or similar document)
- Company's hotline procedures, including process for monitoring complaints received and reporting to AC and/or full board

Information about the AC

- AC charter
- Minutes and pre-read materials from AC meetings for the past year or two
- Materials about upcoming AC activities and meetings

IA materials

- IA charter
- Current-year audit plan

External audit materials

- Current year's external auditor engagement letter
- Management letter (if applicable)
- Recent reports from the external auditor
- Summary of any nonaudit services currently provided by auditor
- Written communications between the AC and external auditors for the past two years
- Summary of financial statements misstatements, including both corrected and uncorrected differences, for the past two years
- Summary of significant control deficiencies and material weaknesses, both remediated and unremediated, for the past two years

Initial orientation session

While the length and formality of a formal orientation session will vary from company to company, it should provide new AC members with an overview of:

- The business – including its products and services, customers, and competitors, as well as the key risks facing the company
- The overall financial status of the company
- The company's near- and long-term strategy
- Expectations for AC members and board members (generally), and an overview of board processes—including meeting schedules for boards and committees, and a copy of the board by-laws
- Risk oversight assignments that are specific to the AC and beyond financial reporting risks
- The company's ethics/compliance program and culture

Who participates in the initial orientation session will vary, depending on how the company's orientation process is structured, e.g., whether the initial orientation is viewed as the first step in a more lengthy process, or whether it is viewed as a more comprehensive orientation session. Depending on the approach, only a few executives might participate in the initial orientation session—e.g., the general counsel, chief financial officer (CFO), chief audit executive (CAE)—or a number of others might participate as well, including perhaps the chief executive officer (CEO), chief risk officer (CRO) or equivalent, controller, and chief compliance officer. The AC chair or lead director may choose to attend as well.

Initial meeting with lead audit engagement partner

A key component of any orientation program for a new AC member is a meeting with the lead audit engagement partner, which should occur early in the orientation process. In addition to obtaining the audit partner's views on a number of critical company-wide issues—e.g., key risks facing the company, effectiveness of risk management processes, overall control environment, strains on the financial reporting system, caliber of the management team, tone and culture of the organization—the new AC member will expect to have an in-depth discussion with the audit partner about a number of specific financial reporting and internal control issues, including:

- Most recent financial statement risk assessment, considering internal and external factors (economy, regulation, accounting standards, competition, etc.)
- Critical accounting policies, i.e., those most sensitive to management's estimating process (reserves, loss contingencies, impairment testing, etc.)
- Prior-year internal control deficiencies and status of remediation efforts
- Most recent year-end unadjusted audit differences reported to the AC and reasons for the differences (GAAP departures, assumptions used by management, hard errors, etc.)
- Overall quality of the company's accounting policies and reporting
- Required communications for the most recent annual and subsequent interim periods
- External auditor's relationship with management and IA
- External auditor's relationship with the AC outside of regularly scheduled meetings (frequency of interaction, accessibility, depth of discussions)
- Quality of the finance organization (including locations outside of headquarters)

- Quality of IA department (skill sets, experience, support of the annual audit)
- Management's approach when preparing to adopt new accounting standards
- Scope of external audit, including approach to multi- and foreign-location components, and use of affiliated or other auditing resources
- Use of audit reports on outsourced service providers
- Use of company's internal and external experts, such as actuaries, valuation experts, and others
- Audit approach to consideration of fraud

Developing a deeper understanding of the company and the board

Regardless of whether it is part of a formal or structured orientation process, a new AC member will want to have one-on-one discussions with a number of key leaders of the business to gain a better understanding of the company—the culture, strategy, key risks, strengths, areas of concern, etc.—and to get to know the leaders outside of the formality of the boardroom.

Initially, it may be helpful to get the "lay of the land" by meeting separately with the general counsel and the CAE, each of whom can be valuable sources of information and insight. What are the hot-button issues facing the company? What issues have management and the board been spending the most time on? What governance processes work well, or not so well? What is the culture of the company and of the board?

The general counsel can provide information about the board from a legal and process point of view, including the committee structure, the role of each committee, and how the committees coordinate and communicate about oversight activities. The general counsel can also provide an update on litigation or investigations that could have an impact on the company's financial statements, disclosures, and legal/regulatory compliance.

With IA increasingly playing a larger role in many businesses, the CAE should also have important insights to offer regarding the effectiveness of the organization's risk management processes, system of internal control, and governance processes. In addition, a new AC member will expect to hear from the CAE regarding:

- Nature and scope of operational audits underway
- Management's cooperation and responsiveness to deficiencies identified as part of audits
- Top operational concerns
- Level of assurance that the company has effective risk management practices in place
- Adequacy of resources for finance team and IA (If IA had an additional 10 percent in its budget, how would it be used?)
- Current stresses and strains on the financial reporting system
- Process for communicating with the AC (frequency, format)

In the weeks and months following the initial orientation session, a new AC member may also want to meet one-on-one with other leaders in the business—CEO, CFO, CRO (or equivalent), AC chair, lead director, chief information officer (CIO)—to get their views on a number of key company-wide issues, including:

- The company's strategic direction and key risks to the strategy
- Effectiveness of risk management processes
- The overall control environment
- Tone and culture of the organization, including ethics/legal/regulatory compliance
- Strengths and weaknesses of the management team and the board

The business leaders also will have important insights to offer on issues that are specific to their areas of focus and responsibility. In the appendix, we identify possible issues to explore.

No "one size fits all"

A good onboarding process—which is key to getting a new AC member up to speed and in a position to contribute to the work of the committee—is not a "one size fits all" process, and may vary considerably, depending on the background, experience, and areas of interest of a new director. While management obviously plays a key role in shaping the onboarding program, every new AC member needs to take charge of his or her own onboarding in order to make sure that it is properly tailored and focused.

Appendix: Other potential discussion topics

CFO and CAO

- The company's earnings trends
- Key financial reporting risks—the pressures and vulnerabilities in the financial reporting process
- Adequacy of control environment, including fraud controls
- Critical accounting estimates
- Level of transparency in the company's financial disclosures
- Role of management's disclosure committee
- Strengths and weaknesses in compliance programs, including FCPA

CRO (or equivalent role)

- How the CRO gains a view of risk across the enterprise and how key risks are aggregated
- Aspect(s) of risk management posing the greatest challenge to the company
- CRO's view of the company's risk awareness, "appetite," and "tolerance"
- How the CRO views the tone and culture of senior management
- How the company's risks compare to others in the industry
- Strengths and weaknesses in the board's risk oversight processes

CIO

- How the company manages data security, compliance, cyber risk, major IT investments, and other "defensive" IT risks
- How the company leverages IT "offensively" for strategic advantage
- Nature and frequency of CIO communications with board/AC
- Company's policies/practices for data governance, use of social media, and adoption of emerging technologies

AC chair

- Expectations and role of the new AC member
- Current composition of the AC (skills, backgrounds, experience, and expertise)
- Most difficult/challenging financial statement issues
- Scope of the AC's oversight responsibilities
- Strength of the AC's oversight processes
- Results of the AC's last two self-assessments

Lead director

- How the board interacts with the CEO and other officers, and how important decisions are made (formal and informal processes)
- Toughest issues facing the board/committees
- Board culture, including openness and candor of communications and debate among management and the board, and among directors

CEO

- Any significant issues or concerns identified by other business leaders
- On what issues does the CEO expect to spend the most time over the next few months?
- How can the skills and background of the new AC member—and board members, generally—be best leveraged for the benefit of the board and the company?

Additional resources and reading:

KPMG's Audit Committee Institute (ACI)
www.kpmg.com/aci

Report of the NACD Blue Ribbon Commission on The Audit Committee

Report of the NACD Blue Ribbon Commission – Risk Governance: Balancing Risk and Reward

Audit Committee Institute

Part of the Board Leadership Center, KPMG's Audit Committee Institute focuses on oversight of financial reporting and audit quality and other issues of interest to audit committee members, including risk oversight, internal controls, and compliance. Learn more at kpmg.com/aci.

About the KPMG Board Leadership Center

The KPMG Board Leadership Center champions outstanding governance to help drive long-term corporate value and enhance investor confidence. Through an array of programs and perspectives—including KPMG's Audit Committee Institute and Private Markets Group, the WomenCorporateDirectors Foundation, and more—the Center engages with directors and business leaders to help articulate their challenges and promote continuous improvement. Drawing on insights from KPMG professionals and governance experts worldwide, the Center delivers actionable thought leadership—on risk and strategy, talent and technology, globalization and compliance, financial reporting and audit quality, and more—all through a board lens. Learn more at www.kpmg.com/blc.

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