

**COUNTY OF MONTEREY BOARD OF SUPERVISORS
AUDIT COMMITTEE CHARTER SUPPLEMENTAL**

Introduction

A public-sector audit committee plays a critical role supporting the Board's responsibility of overseeing government resources. Public-sector Audit Committees serve as an independent oversight and advisory role to their respective Boards. Audit Committees are primarily responsible for ensuring effective oversight of governance, risk management, and internal control practices. They achieve this by facilitating decision making and ensuring a system of oversight, management and control is implemented and high-quality internal and external information is reported.

Guidance to Audit Committee Criteria**A: Mandate****Background**

This section should come from laws, regulations, board orders, policies and procedure or bylaws. Internal Audit has been unable to find direct authority under California's Government Code that discusses the establishment of an Audit Committee within local governments.

The Institute of Internal Auditors

"Regardless of how the mandate is established, good governance dictates that public-sector entities have an independent audit committee and its members are established in legislation and/or regulation."

"A written charter should establish the audit committees mandate..."

Government Finance Officers Association

"The governing body of every state and local government should establish an audit committee or its equivalent."

"The audit committee should be formally established by charter..."

Recommendation

Although strongly recommended, establishing an Audit Committee for the County of Monterey appears to be at the Board's discretion. In doing so, the Board must consider best practices and ensure the Audit Committee is independent and contains adequate expertise. (See discussion on "Committee Members: Independence and Expertise; Critical Factors" below)

B: Committee Members: Independence and Expertise; Membership Critical Factors**Background**

The role of the Audit Committee is to support the Board in fulfilling its oversight responsibilities. They do this by providing objective advice and recommendations on

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whether the organization's governance, risk management, and internal control processes are suitably designed and working as intended. Requisite to this is the leading practice of having audit committee members be independent of management responsibilities and contain expertise in subject matter of comparable entities.

Independence: It is critical that the composition of the Audit Committee have a majority of independent external members. An independent member is a person who is not employed by, or providing any services to, an organization beyond his or her duties as a committee member.¹

Expertise is essential to a well-functioning audit committee. To ensure adequate expertise is present with the audit committee, the audit committee should contain at least one member who is a financial expert meaning one who is familiar with generally accepted auditing standards, has experience preparing or auditing financial statements of comparable entities, or has experience in apply accounting principles related to estimates, accruals and reserves.

Independence and expertise are critical factors to ensuring the effectiveness of the audit committee and are strongly recommended by the following authoritative bodies:

The Institute of Internal Auditors

"An essential feature of an effective audit committee is independence from management. By providing an independent source of advice to the board, audit committees play a key role in an organizations governance structure. To ensure audit committee independence, it is a leading practice for the majority of members to be independent. An independent audit committee member is a person who is not employed by, or providing any services to, the organization beyond his or her duties as a committee member."

"In addition to being independent from the organization, audit committee members are expected to... collectively be knowledgeable of, or have expertise in, finance and accounting, business, auditing risk management, compliance, and information technology"

"As a leading practice, many organizations require that an audit committee include at least one person who is a financial expert."

Association of Local Government Auditors

Members should be independent of management. To enhance the independence of the committee, and to enable the auditors to communicate freely about management's shortcomings, no member of the audit committee should be employees of the entity management (executive branch).

"We recommend that audit committees include both members of the legislative body and financial/management experts from the community."

¹ As defined by the IIA ACGA

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Government Finance Officers Association

“No governing body member who exercises managerial responsibilities that fall within the scope of the audit should serve as a member of the audit committee.”

“The audit committee should have access to the services of at least one financial expert. Such a financial expert... possess 1) an understanding of the generally accepted accounting principle and financial statements; 2) experience in preparing or auditing financial statements of comparable entities; 3) experience in apply such principles in connection with the accounting estimates, accruals and reserves, 4) experience with internal accounting controls; and 5) an understanding of audit committee functions.”

“An audit committee should have sufficient members for meaningful discussion and deliberation, but not so many as to impede its efficient operation. As a general rule, the minimum membership of the committee should be no fewer than three.”

Internal Audit Recommendation:

It is recommended that a five-member Audit Committee be established comprising of two Board Supervisors and three independent members from the community. Expertise attributes to be included in audit committee membership must ensure:

- 1) Members possess or obtain a basic understanding of government financial reporting and auditing;
- 2) Members should have knowledge of governance, risk and internal controls;
- 3) Members should have access to the services of at least one financial expert, which is either a committee member or an outside party.

C: Terms of Office

Background

Because the responsibilities of the audit committee evolve in response to regulatory, economic, and reporting developments, it is important to periodically re-evaluate members' competencies and the overall balance of skills on the committee in response to emerging events. The Audit Committee should establish the terms of service/number of years' members are assigned to serve on the Committee. Three to four years is typical. Committee members should be periodically evaluated in relation to meeting the Committee's needs.

Authoritative bodies emphasize the need to establish definitive durations for audit committee membership and importance of maintaining continuity as follows:

The Institute of Internal Auditors

“It is important that audit committees maintain institutional memory while providing new perspectives and fresh insights. Audit committee members should, therefore, be appointed to terms long enough to maintain continuity but no so long that an individual becomes vested in the organizations current policies and direction.”

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Association of Local Government Auditors

“Terms of audit committee members should be staggered to ensure continuity.”

Government Finance Officers Association

“The written documentation establishing the audit committee should prescribe the scope of the committee’s responsibilities, as well as its structure, processes, and membership requirements.”

Internal Audit Recommendation

The Board should establish a 4-year service period for audit committee members. Board members serving on the audit committee should do so over the duration of their elected term. Independent/external audit committee members should serve staggered terms to ensure continuity on the committee.

D: Committee Values

Background

Because of their role and responsibilities of overseeing governance, risk and control activities, Audit Committee members should exhibit superior ethics and values and show the highest concern for compliance with laws, regulations and policies and procedure designed to ensure ethical practices. The Committee should consider developing and expressing values and ethics policy and how those values help to achieve, or support, the Committee’s activities.

The Institute of Internal Auditors

“In addition to being independent from the organization, audit committee members are expected to conduct their work in a diligent and professional manner; demonstrate inquisitiveness, outspokenness, and courageousness...”

Internal Audit Recommendation

The audit committee should develop a formal values and ethics statement and supporting policies framed around the Audit Committee’s scope and objectives. Values policies should emphasize the importance of effective governance, risk awareness, internal controls, compliance with state and federal laws and regulations, compliance with County policies and procedures, professional ethical conduct etc.

E: Meetings

Background

The Committee should establish a schedule for when they will meet. It is recommended the Committee meet at least once a quarter for a minimum of four meetings a year.

The Institute of Internal Auditors

“Leading practice recommends meeting at least four times a year.”

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“At least annually, the audit committee shall hold a private session with the chief executive officer, chief financial officer, the chief audit executive, external assurance providers and with any other officials that the audit committee may deem appropriate.”

Internal Audit Recommendation

The audit committee meet at a minimum once every quarterly for a total of four meetings per year. Meetings should be considered for content with sensitive information or information containing personally identifiable information discussed during closed session.

F: Remuneration of Committee Members

Background

Once the Board decides on the composition of the Audit Committee remuneration and indemnity insurance of external members should be considered and documented in the Audit Committee Charter. Indemnity insurance, also referred to as professional liability insurance, is a supplemental form of liability insurance specific to certain professionals or service providers. Such professionals provide counsel, expertise, or specialized services. Indemnity insurance protects audit committee members from bearing the full cost of defending against a negligence claim.

Internal Audit Recommendation

The Audit Committee should establish policy and procedures of providing remuneration and indemnity insurance to external audit committee members. Both compensation and indemnity insurance should be considered in relation to laws, regulations, or in written policy and procedures by the governing body.