

### Audit Committee Roundup

# Making the Most of Executive Sessions

By Edward F. Smith

Candor and unvarnished viewpoints are tremendously important to the audit committee in its oversight role, which is why executive sessions are now standard fare for audit committees. What's not standard is the value and insight that these sessions produce: Many audit committees continue to wrestle with various factors—like timing and frequency, what's discussed, who participates, and follow-through with management—that can help, or hamper, the committee's efforts to get the most out of executive sessions.

With this in mind, here are four commonly asked questions, and some suggestions for making the most of audit committee executive sessions:

**1.** How often and when should executive sessions be held?

Avoid negative inference about the calling of executive sessions by holding them, as a matter of routine, at all audit committee meetings. Most audit committees hold executive sessions immediately *after* committee meetings to privately discuss topics that were addressed during the meeting, as well as other issues they prefer to discuss without management present. These sessions might last several minutes or much longer; the key is to ensure the discussions are not rushed or inhibited by artificial time constraints. Committee members should plan their schedules accordingly.

Consider also holding brief executive sessions prior to audit committee meetings, as a “pre-discussion” of sensitive topics or to consider whether changes should be made to the meeting agenda once committee members have reviewed pre-meeting materials.

**2.** Who should attend?

An “audit committee member only” portion of the executive session provides an opportunity to privately discuss the performance

of the financial-management team—including the adequacy of communications from the team—as well as compensation, succession planning, and any other concerns that surfaced during the meeting. It also provides an opportunity to deliberate and reach consensus on difficult issues.

The NYSE's corporate governance rules require the audit committee to hold periodic, private sessions with management, independent auditors, and internal auditors, and a portion of the executive session should be devoted to these talks. One-on-one meetings with the CFO, the internal auditor, and the external auditor are intended to encourage candor and open communications, and provide an opportunity to discuss difficult issues about management and auditor performance. Some audit committees make it a point also to have periodic private sessions with managers below the CFO level, to assess whether information the committee receives is open and transparent, and not “overly controlled” by senior management.

Most audit committees also have periodic private one-on-one meetings—at least annually—with others, such as the CEO, general counsel, and compliance and risk officers.

**3.** What should be on the agenda?

Executive sessions often have no planned agenda. This private session is an opportunity for a frank and open-ended discussion: to clarify confusing issues or facts, ask questions, express doubts, voice opinions, and generally have the type of conversation not possible with management present. An important role for the audit committee chair is to set the tone and encourage such discussions.

When meeting one-on-one with management and auditors, audit committee

members generally pose questions to elicit any concerns about management or auditor competency, resources, or candor, as well as both general and specific concerns about the financial reporting and control environment. At times, the audit committee chair may provide managers or auditors with a question in advance, so they have an opportunity to consider the issue more fully before the session. Of course, members need to be prepared to ask follow-up questions and “test the answers,” and take action to address any issues.

**4.** What type of follow-up and documentation is appropriate?

It's generally left to the audit committee chair to communicate with management or auditors the issues or concerns identified during the executive session that may require their attention and follow-through. In addition, the chair should report to the lead director or board as appropriate. While opinions vary about the scope of documentation for executive sessions, it's generally recognized that some level of documentation is important. (Audit committee chairs should confer with counsel—who may or may not have attended the executive session—to determine what level of detail may be appropriate for each executive session.)

Finally, recognize there's no single “best approach” to executive sessions. The degree of candor and quality of communication—from all participants—is the best indicator of whether executive sessions are working well, or are in need of adjustments.



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