Resource Management Guide No. 202
Audit committees for Commonwealth entities and Commonwealth companies

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This guide contains material that has been prepared to assist Commonwealth entities and companies to apply the principles and requirements of the Public Governance, Performance and Accountability Act 2013 and associated rules, and any applicable policies. In this guide the: mandatory principles or requirements are set out as things entities and officials ‘must’ do; and actions, or practices, that entities and officials could do to give effect to those principles and/or requirements are set out as things entities and officials ‘should consider’ doing.
**Audience**

This guide is relevant to accountable authorities of Commonwealth entities, governing bodies of Commonwealth companies and audit committee members.

**Key points**

This guide:

- details considerations for establishing and operating an audit committee to provide independent advice and assurance to accountable authorities and governing bodies
- provides guidance to accountable authorities and governing bodies on determining the audit committee's charter, including the review of the integrity of the entity's financial and performance reporting and compliance requirements
- comes into effect immediately to support the implementation of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) and the *Public Governance, Performance and Accountability Rule 2014* (PGPA Rule), which take effect on 1 July 2014.

**Resources**

This guide is available on the Department of Finance website at www.finance.gov.au.

Other relevant publications include:

- Australian National Audit Office, *Public sector audit committees: independent assurance and advice for accountable authorities* (Better Practice Guide, March 2015), which has informed this guidance, in particular the sections on ‘Skills and experience required of audit committee members’ and ‘Contractual arrangements and remuneration’.
Public Governance, Performance and Accountability Act 2013

Section 45—Audit committee for Commonwealth entities

1. The accountable authority of a Commonwealth entity must ensure that the entity has an audit committee.

2. The committee must be constituted, and perform functions, in accordance with any requirements prescribed by the rules.

Section 92—Audit committee (for Commonwealth companies)

1. The directors of a wholly-owned Commonwealth company must ensure that the company has an audit committee.

2. The committee must be constituted, and perform functions, in accordance with any requirements prescribed by the rules.

Public Governance, Performance and Accountability Rule 2014

Section 17—Audit committee for Commonwealth entities

Guide to this section

The purpose of this section is to set out minimum requirements relating to establishing an audit committee for a Commonwealth entity to help ensure that the committee provides independent advice and assurance to the entity’s accountable authority. While an audit committee needs to be established for each Commonwealth entity, and the accountable authority must determine the functions the committee is to perform for the entity, this section does not prevent the same audit committee being established for multiple Commonwealth entities.

This section is made for subsection 45(2) of the Act.

Functions of the audit committee

1. The accountable authority of a Commonwealth entity must, by written charter, determine the functions of the audit committee that is established for the entity as required by subsection 45(1) of the Act.

2. The functions must include reviewing the appropriateness of the accountable authority’s:

   (a) financial reporting; and
   (b) performance reporting; and
   (c) system of risk oversight and management; and
   (d) system of internal control;
   for the entity.
Membership of the audit committee

(3) The audit committee must consist of at least 3 persons who have appropriate qualifications, knowledge, skills or experience to assist the committee to perform its functions.

(4) On and after 1 July 2015, the majority of the members of the audit committee must:
   (a) for a non-corporate Commonwealth entity—be persons who are not officials of the entity; or
   (b) for a corporate Commonwealth entity—be persons who are not employees of the entity.

(5) Despite subsections (3) and (4), the following persons must not be a member of the audit committee:
   (a) the accountable authority or, if the accountable authority has more than one member, the head (however described) of the accountable authority;
   (b) the Chief Financial Officer (however described) of the entity;
   (c) the Chief Executive Officer (however described) of the entity.

Section 28—Audit committee for wholly-owned Commonwealth companies

Guide to this section
The purpose of this section is to provide that the requirements in section 17 of this rule about establishing audit committees of corporate Commonwealth entities also apply to audit committees of wholly-owned Commonwealth companies. This is to help ensure that audit committees of wholly-owned Commonwealth companies provide independent advice and assurance to the governing bodies of those companies.

This section is made for section 92 of the Act.

(1) Section 17 of this rule (which is about audit committees for Commonwealth entities) applies to a wholly-owned Commonwealth company in the same way as it applies to a corporate Commonwealth entity.

(2) For the purposes of subsection (1), a reference in section 17 to the accountable authority of the entity is taken to be a reference to the governing body of the company.

Introduction

1. An independent audit committee is an important element of good governance. Audit committees provide independent advice and assurance to the accountable authority of an entity on the appropriateness of the entity's accountability and control framework, including to independently verify and safeguard the integrity of an entity's financial and performance reporting. Section 45 of the PGPA Act requires an accountable authority of a Commonwealth entity to ensure that their entity has an audit committee. Commonwealth companies are also required to have an audit committee under section 92 or the PGPA Act.

2. The PGPA Rules set out minimum requirements relating to establishing an audit committee for a Commonwealth entity and a Commonwealth company (sections 17 and 28 of the PGPA Rule respectively). These rules aim to help ensure that the committee provides independent advice and assurance to the entity's accountable authority or the company's governing body.
(hereafter referred to collectively as the accountable authority). While an audit committee needs to be established for each Commonwealth entity or company, and the accountable authority must determine the functions the committee is to perform for the entity, section 17 does not prevent an audit committee from providing its services to multiple Commonwealth entities.

**Functions of audit committee**

3. The accountable authority must, by written charter, determine the functions of the audit committee. That charter should also include particulars of the committee’s:
   - meeting frequency
   - membership
   - quorum arrangements.

4. The functions of the audit committee that are outlined in the charter must include, at a minimum, reviewing the appropriateness of the accountable authority’s:
   - **financial reporting,** which may cover
     - advising the accountable authority on the preparation and review of the entity’s annual financial statements
     - providing any other advice to the accountable authority about the accountable authority's obligations under the PGPA Act and other relevant Acts
     - advising the accountable authority on the adequacy, framework and controls relating to the entity’s internal budgeting and reporting
   - **performance reporting,** which may cover
     - reviewing the framework for the selection of key performance indicators and other performance measures
     - advising the accountable authority on the preparation and review of the entity’s annual performance statement
     - advising the accountable authority about action that could be taken on significant matters of concern or significant opportunities for improvement that are mentioned in reports of internal and external audits
   - **systems of risk oversight and management,** which may cover
     - advising the accountable authority about the internal audit plans of the entity
     - advising the accountable authority about the professional standards to be used by internal auditors in the course of carrying out audits in the entity
     - as far as practicable, coordinating work programmes relating to internal and external audits
     - reviewing the adequacy of the entity’s response to reports of internal and, as far as practicable, external audits
     - reviewing the content of reports of internal and external audits to identify material that is relevant to the entity, and advising the accountable authority about good practices
     - reviewing the entity’s risk management framework including:
       - the entity’s risk management plan
       - the entity’s business continuity plan
• *systems of internal control,* which may cover
  – reviewing the adequacy of the controls that are designed to ensure the entity’s compliance with legislation
  – reviewing the adequacy of the entity’s governance arrangements
  – reviewing the adequacy of the entity’s internal control environment.

5. The functions of the audit committee do not need to be limited to those listed above. The accountable authority should consider if the audit committee could also be utilised for a broader range of functions, such as combining the audit and risk committee functions together. This has the benefit of enabling a broader view of the entity, while also decreasing the number of committees and members the entity will need to support.

### Independence of audit committee members

6. The distinguishing feature of an audit committee is its independence. The committee’s independence from the day-to-day activities of management helps to ensure that it acts in an objective, impartial manner, free from conflict of interest, inherent bias or undue external influence.

7. Appointing a majority of external members to the committee is the most visible and practical way to make sure the committee is as independent as possible from the management of the entity.

8. An independent member cannot be an official or employee of the entity. Board members of corporate Commonwealth entities or Commonwealth companies are not employees of the entity and are therefore considered to be independent. To avoid doubt, an audit committee for a corporate Commonwealth entity may include independent persons who are not board members.

9. Section 17 of the rule provides for a transition period before the requirement to have a majority of independent committee members comes into effect on 1 July 2015. Entities that are in a position to move towards majority independent membership before that date should take steps to do so.

10. Other measures to strengthen the committee’s actual or perceived independence include:

    • appointing an independent chair—as the most influential member of the audit committee, an independent chair can perform their role unencumbered by any management responsibilities and can give the accountable authority advice and assurance from an independent perspective
    • not appointing committee members who will favour a particular area within the entity
    • having a rotation policy for committee members to enable new knowledge and experience to be introduced to the committee
    • having policies in place to facilitate timely identification of changing relationships or circumstances that may affect the independence of committee members.

11. There may also be benefits in appointing a member from another Commonwealth entity as an independent member, particularly when the entities have working relationships or when a person has particular expertise in an area of audit committee responsibility. The need for appropriate privacy, confidentiality and conflict-of-interest provisions should be considered in these circumstances.
Persons excluded from being audit committee members

12. To ensure ongoing independence, section 17(5) of the rule excludes the chief financial officer, the chief executive officer (however described), and accountable authority—or, if the accountable authority consists of two or more people, the person who is the head (however described) of the accountable authority—from being members of the audit committee.

13. Also, it is advisable that the chief operating officer, the chief information officer, the head of the corporate services area, and the head of internal audit not be members of the audit committee.

14. Nevertheless, it may be appropriate for the chair, chief executive officer or chief financial officer to attend meetings as an observer. It is well recognised that this can contribute to the overall workings of the audit committee.

Skills and experience required of audit committee members

15. The audit committee must include people who have appropriate qualifications, knowledge, skills or experience to assist the committee to perform its functions. Members should be financially literate (that is, able to read and understand financial statements). At least one member of the committee should have accounting or related financial management experience and/or qualifications, and a comprehensive understanding of accounting and auditing standards. Collectively, the audit committee should possess broad business, financial management and/or public sector experience, and general knowledge of most of the areas listed in the following paragraph.

16. Audit committee members should collectively have knowledge or expertise in:
   - the business or industry in which the entity operates
   - risk identification, evaluation and management
   - project and programme management
   - information management and security
   - the operations of government and the public sector, including information technology systems and controls
   - the roles of internal and external audit
   - the application of accounting, auditing and assurance standards
   - relevant legislative and other policy requirements of the entity
   - public sector reporting requirements, including financial and performance reporting
   - internal control, compliance activities and fraud control.

17. The audit committee must consist of at least three persons. The size will depend on the nature and extent of its responsibilities, but it commonly comprises three to six members.

Contractual arrangements and remuneration

18. When procuring the services of external members of the audit committee, non-corporate entities (and prescribed corporate Commonwealth entities listed in the Commonwealth Procurement Rules) must comply with the Commonwealth Procurement Rules where applicable. When accepting an appointment to serve on an audit committee, external
members and the entity should ensure that the contractual arrangements clearly outline the role and the terms and conditions of appointment. This should include any requirements relating to hours to be worked, indemnity insurance, signing of conflict of interest declarations, remuneration and any specific requirements, so members and entities fully understand their obligations.

19. External committee members should be remunerated at a level that reflects the time it takes to effectively meet their responsibilities. Allowance should be made for the particular skills and expertise a member will bring to the committee, and the time required for meeting preparation, attendance at meetings and interaction with management outside committee meetings. Recognition should also be made for the additional responsibilities of the chair.

Sharing audit committees between agencies

20. The rule has been designed to encourage, where practicable, the sharing of audit committees or members of audit committees. This supports independence and sharing of better practice among entities. The sharing of members between the audit committees of entities can also help to reduce operating costs and improve the utilisation of high-calibre committee members.

21. An effective way to reduce costs and improve independence is to create a single audit committee from senior executive service officers from several agencies. This group can then be utilised as the audit committee for each agency that contributed an officer. This group could be supplemented by an external member or chair with expertise in audit committees.

Further information

22. For further information on how an accountable authority can identify suitable people for inclusion on an entity's audit committee, please contact the Department of Finance.