Kate Sayer: When you should have a separate audit committee

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It pays to avoid the danger that your finance committee becomes a shadow board, writes our columnist

Kate Sayer

Is it necessary to have a separate audit committee if you have a finance committee that combines both functions? There are no hard-and-fast rules, but it is worth paying attention to a few key principles.

Finance committee

A finance committee oversees the process of planning and reporting the finances of the organisation. It should ensure timely budgeting with appropriate involvement from other functions. It scrutinises the draft budget and validates the assumptions underpinning it. It reviews financial reports and monitors financial performance. The treasurer commonly chairs the committee.

The committee must ensure an organisation maintains relevant finance policies. It should scrutinise important financial strategies such as the reserves, investment and grant-making policies. Other aspects of financial strategy are within its remit - such as pricing, how the organisation handles new business and investment - if there is no separate investment committee.

Audit committee

The audit committee should oversee the risk management process, so it's often called the "audit and risk" committee. It ensures the organisation identifies, assesses and manages risks effectively, and reviews whether internal audit is needed to provide assurance on the effectiveness of controls. If there is no internal audit function, it should ensure it gets assurance on effective internal controls from management. For example, it would review the business continuity plan on behalf of the board.

The role of the committee encompasses scrutiny of decision-making processes and all governance processes, including policy-setting. It must therefore be independent. For the same reason, the treasurer should not chair the audit committee, but may be a member of it. An audit committee might need information from finance, so attendance by the treasurer is the simplest way to ensure good communication.

Combined committee

Smaller charities typically have one committee for finance and audit. In practice, they do not take on the whole audit committee role, but do have responsibility for the appointment of external auditors and receive their reports. Other functions of the audit committee, such as risk management, are usually handled by the full board. Similarly, if you do not have a separate remuneration committee, this function reverts to the whole board.

If you do have a combined committee, I try not to let it become the working group for all matters. There is a danger that the finance committee becomes a shadow board, with decisions made in the committee on matters that should be brought before the whole board. The board has to provide oversight and scrutinise finance and risk matters. A board that leaves everything to the finance committee might wake up to a nasty surprise one day.

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