

Comptroller of the Treasury
Division of County Audit
Audit Committee Guidelines
September 2010

These guidelines were developed for local governments to establish an Audit Committee under provisions of Tennessee Code Annotated (TCA), Section 9-3-405.

Background

The Local Government Modernization Act of 2005 (TCA, Section 9-3-405) provides for the establishment of an audit committee in local governments. This statute encourages local governments to consider establishing an audit committee and under certain conditions the comptroller may require that an audit committee be established. The two conditions are when a local government is in non-compliance with the accounting and financial reporting standards required by the Governmental Accounting Standards Board or a local government has recurring findings from the annual audit for three (3) or more consecutive years as determined by the comptroller to be a material weakness in internal control or material noncompliance under government auditing standards.

Purpose of Audit Committee

The audit committee is established to provide independent review and oversight of the government's financial reporting processes, the government's internal controls, and a review of the external auditor's report and following up on corrective action, and compliance with laws, regulations, and ethics.

Audit Committee Guidelines

- 1) The legislative body shall approve the resolution or charter establishing an audit committee.
- 2) The audit committee members shall be external to management. The members may be members of the governing body, citizens of the local government , or a combination of both. The members should be appointed by the legislative body for staggered terms. There should be no fewer than three members on the committee.
- 3) The members should possess sufficient knowledge and experience in finance, business, and accounting to discharge the committee's duties.
- 4) The resolution or charter shall provide for the responsibilities and duties of the committee. These duties shall address financial and other reporting practices, internal control, compliance with laws, regulations, and ethics.

- 5) The resolution or charter creating the duties and responsibilities of the audit committee shall be submitted to the comptroller prior to approval by the legislative body. The comptroller shall review the proposed resolution or charter and report back to the local government on whether it follows recommended guidelines. The resolution or charter adopted by the legislative body must conform to the report issued by the comptroller.
- 6) The audit committee shall provide a written report to the legislative body each year on how it has discharged its duties.
- 7) The audit committee shall establish a process for handling employees, taxpayers, or other citizens confidential reporting of suspected illegal, improper, wasteful, or fraudulent activity under provisions of TCA, Section 9-3-406.
- 8) The audit committee should carefully review all audit findings in the audit report and have consultation with the external auditor regarding the irregularities and deficiencies disclosed in the annual audit. The committee should satisfy itself that appropriate and timely corrective action has been taken by management to remedy the identified weaknesses. The committee should determine what corrective action, if necessary, should be recommended to the legislative body.
- 9) The meetings of an audit committee shall abide by the notice requirements adhered to by the local government to which the committee is attached, except as provided in subsection (d) of TCA, Section 9-3-405.
- 10) All meetings of the audit committee shall be subject to the meeting provisions of subsections (d),(e),(f),(g),(h), and (i) of TCA, Section 9-3-405.

Audit Committee and the Internal Audit Function

In many larger governments there is an established independent internal audit function. In those governments that establish such an internal audit function the audit committee must always be afforded access to the internal audit annual work plan, as well as to any and all individual audit reports.

There are varying positions on the reporting relationship between the audit committee and the internal audit function. One position is to have the internal audit function completely independent of management and therefore report directly to the audit committee. Another position is to have the internal audit function report to the audit committee and administratively to the county mayor/county executive.

In smaller governments it may not be practical to establish a formal internal audit function. In that case, the local government may consider either assigning internal audit responsibilities to its regular employees or obtaining internal audit services from an accounting firm.

If a local government establishes an internal audit function, the charter for its operations should be tied to the charter of the audit committee.