



VIEWS ON THE ROLE OF AUDIT COMMITTEE IN CORPORATE GOVERNANCE

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Abstract: *The Audit Committee is a structure which has consulting role for the Management Board or for the Supervisory Board. The Audit Committee is composed only of non-executive administrators' independent from the executive management. The Audit Committee will support the Management Board in the monitoring of credibility and integrity of financial information provided by the company, especially by the revision of relevance and consistency of accounting standards applied by the company. The Management Board or the Audit Committee, as applicable, will regularly examine the efficiency of financial reporting, internal control and risk management system adopted by the company. The Audit Committee will meet whenever it is necessary, but at least twice a year, on the occasion of drawing up the semestrial and annual statements, when the Committee assures their dissemination to shareholders and the general public. The Audit Committee reports every year to the Management Board or the Supervisory Board regarding the activity carried out during the previous year and whenever it considers appropriate or necessary for the fulfilment of its responsibilities.*

Key words:

Unitary system of corporate governance, dual system of corporate governance, obligatory character of Audit Committee, necessity of Audit Committee, role of Audit Committee.

JEL Codes:

M40, M41

1. Introduction

Through the hereby study we set ourselves on an analysis over the views on the role of Audit Committee in corporate governance. The Companies Law no. 31/1990, further amended, provides the possibility of creating the Audit Committee, which has the responsibility of conducting investigations based on which it can make recommendations for the Management Board, but does not detail the status, assignments and mode of operation of this committee. According to companies law, the joint-stock companies whose annual financial statements make the object of a legal obligation of auditing, the foundation of an Audit Committee in the Management Board is obligatory. The Government Emergency Ordinance no. 90/2008 regarding statutory audit provides the obligation of public interest entities to have an Audit Committee.

2. Romanian model of corporate governance

In Romania the elements of corporate governance were imposed by the Companies Law no. 31/1990. The norms and principles of organization and management of companies in Romania were reviewed and subsequently supplemented, assuring the legal framework for the implementation of corporate governance requirements. The legal framework of Romania provides two models or systems of corporate governance of joint-stock companies, except for those which according to Law

no. 346/2004 are considered SMEs (Lenghel, R.D. 2013 pp: 74): a) unitary system; b) dual system.

a. Unitary system of corporate governance

The joint-stock companies are governed by a Board of Directors and a sole administrator appointed by the General Meeting of Shareholders (GMS), for a period of maximum four years.

The joint-stock companies whose annual financial statements are obligatorily subjected to auditing are managed by at least three administrators. During their mandate, the administrators cannot conclude employment agreement with the company.

The Board of Directors can delegate the company management assignments to one or several directors, appointing one of them managing director. The directors can be appointed among the administrators or from outside the Management Board. Most of the members of the Management Board must be non-executive administrators (among persons who do not hold the position of executive director). With the approval of the General Meeting of Shareholders, the president of the Management Board can also be appointed managing director.

The Management Board meets at least every 3 months. The directors and internal auditors or, as applicable, the auditors can be summoned to participate, without voting right, to the works of the Management Board.

The Management Board fulfils all the necessary acts for the fulfilment of the object of activity of the company, except for the acts reserved for the General Meeting of Shareholders. The main competences of the Management Board are (Lenghel, R.D. 2013 pp: 75):

- establishes the main directions of activity and development of the company;
- approves the accounting system and the internal control system as well as the financial plan;
- oversees the good functioning of the bodies of the company and supervises the activity of directors;
- organizes the General Meetings of Shareholders, presents reports to shareholders and implements their decisions;
- appoints and revokes directors and establishes their remuneration;
- represents the company in the relations with third parties and in court.

The Management Board can create consultative committees made of at least two members of the board. At least one member of each committee must be an independent non-executive administrator. The consultative committees carry out investigations, elaborate recommendations and reports for the Management Board in the fields of internal and external audit, remuneration of administrators, directors and staff or the nomination of applicants for the management positions.

The audit committee and the remuneration committee are made only of non-executive administrators. At least one member of the audit committee must have experience in the application of accounting principles or in the field of financial audit.

If the financial statements make the object of a legal obligation of auditing, the creation of the audit committee is obligatory.

b. Dual system of corporate governance

By articles of association or by the decision of the General Meeting of Shareholders it can be established that the joint-stock companies are governed through two levels: 1) – Board of Directors; 2) – Supervisory Board.

1) Board of Directors

The management of the joint-stock companies is the exclusive responsibility of the Board of Directors, except for those acts which are reserved by law to the Supervisory Board or the General Meeting of Shareholders.

If the annual financial statements make the object of a legal obligation of auditing, the Board of Directors is made of at least three members.

The appointment of members of Board of Directors is done by the Supervisory Board, which appoints one of them in the position of president of Board of Directors.

The members of the Board of Directors cannot be simultaneously members of the supervisory board or employees of the company.

The legal provisions synthesized above regarding the members of the Management Board regarding the duration of mandate and their rights and obligations are generally applicable to the members of Board of Directors.

At least every three months, the Board of Directors presents to the Supervisory Board written reports regarding the activity carried out, the results obtained and the events which could influence the fulfilment of objectives of the company.

The Board of Directors presents to the Supervisory Board the annual financial statements audited, the annual report and the profit allocation proposals.

2) Supervisory Board

The General Meeting of Shareholders appoints and revokes the members of the Supervisory Board. The number of members of the Supervisory Board cannot be lower than 3 and higher than 11.

The members of the Supervisory Board cannot be simultaneously members of the Board of Directors or employees of the company, they must be professionals and must observe the independence criteria shown above. The Supervisory Board cannot receive company management assignments, but can have the competence to approve certain types of operations. The Supervisory Board can create consultative committees in the same conditions as shown regarding the Management Board.

The Supervisory Board has the following main assignments (Lenghel, R.D. 2013 pp: 76):

- exerts permanent control over the management of the company by the Board of Directors;
- appoints and revokes the members of the Board of Directors;
- checks the compliance with the legal provisions and the decisions of the General Meetings of Shareholders;
- reports to the General Meetings of Shareholders on the supervisory activity carried out.

The members of the Management Board, the members of the Board of Directors and the members of the Supervisory Board must conclude professional liability insurance.

The remuneration of members of Management Board or the members of Supervisory Board is decided by the General Meeting of Shareholders.

The General Meeting of Shareholders can decide to initiate legal action when the damages are caused to the company by the fault of administrators and directors, respectively by the fault of the members of Board of Directors and Supervisory Board or by the fault of auditors or statutory auditors.

3. Obligatory character, role and assignments of the Audit Committee

The Audit Committee is a structure which has consulting role for the Management Board or for the Supervisory Board. As shown above, the Audit Committee is made only of non-executive administrators independent from executive management. At least one member of the Audit Committee must be a professional in the field of accounting or financial audit. The Audit Committee carries out its activity based on a regulation policy approved by the Management Board or by the Supervisory Board.

By this regulation policy the following are established: composition, assignments and responsibilities of the Audit Committee; periodicity of meetings of members of this committee with executive directors, internal auditors or with other persons; periodicity and content of reporting to the Management Board and other necessary elements for the assurance of observance of corporate governance principles.

The Audit Committee will support the Management Board in the monitoring of credibility and integrity of financial information provided by the company, especially by the revision of relevance and consistency of accounting standards applied by the company.

The Management Board or the Audit Committee, as applicable, will regularly examine the efficiency of financial reporting, internal control and risk management system adopted by the company.

The Audit Committee will meet whenever it is necessary, but at least twice a year, on the occasion of elaboration of semestrial and annual statements, when the Committee will assure their dissemination to shareholders and the general public.

The Audit Committee reports every year to the Management Board or the Supervisory Board regarding the activity carried out during the previous year and whenever it considers appropriate or necessary for the fulfilment of its responsibilities.

The Companies Law no. 31/1990, further amended, provides the possibility of creating the Audit Committee, which has the responsibility of conducting investigations based on which it can make recommendations for the Management Board, but does not detail the status, assignments and mode of operation of this committee. According to companies' law, the joint-stock companies whose annual financial statements make the object of a

legal obligation of auditing, the foundation of an Audit Committee in the Management Board is obligatory. The Government Emergency Ordinance no. 90/2008 regarding statutory audit provides the obligation of public interest entities to have an Audit Committee. The main assignments of this Audit Committee are:

a. to assure that the executive directors fulfil their assignments with responsibility and devotion. In this respect, it monitors the compliance of executive management with the requirements of the legal norms and the ethical and professional codes and with the decisions of shareholders and administrators. A special attention is paid to the evaluation of activity of executive management in the line of risk management, which can threaten the fulfilment of objectives;

b. monitors the efficiency of internal control, internal audit and statutory audit from the entity, monitoring which is carried out by:

- sees to the selection of statutory auditors and heads of internal audit department, watching the assurance of their independence;
- approves the Charta or regulation policy by which the internal audit carries out its activity and sees to the assurance of resources and necessary conditions for the internal audit to achieve its objectives;
- monitors the activity of internal and statutory auditors;
- is a mediator between internal audit/statutory audit and the executive management of the entity. It analyses and proposes the resolution of possible disagreements between them;
- receives the internal audit reports, analyses and periodically approves the observations and recommendations of internal audit and the plans for their implementation;
- receives from internal auditors, statutory auditors and from other persons, written or verbal notifications regarding the shortcomings of internal control and of the risk management process;
- oversees the way in which the proposals or reserves of statutory auditors are analysed and solved;
- makes sure that the Board of Directors takes the remedy measures necessary to resolve the deficiencies identified in the internal control activity and other problems identified by the internal or statutory auditors;
- formulates recommendations to the Board of Directors or the Supervisory Board regarding the strategy and policy of the entity in the field of internal control, internal audit and statutory audit.

c. supervises or monitors the process of elaboration of financial or other type of reports. For the assurance of transparency and accuracy of accounting information, it participates in the selection of accounting policies and in the checking of reports, which are made available to the General Meeting of Shareholders or to the Management Board.

d. presents semestrial and annual reports on its activity to the Board of Directors or the Supervisory Board and whenever it considers appropriate or necessary for the fulfilment of its responsibilities.

4. Conclusions

In relation to the role of the audit committee in corporate governance, we can draw the following conclusions:

- in the business environment of Romania we cannot speak of a full awareness of the necessity and role of the audit committee, regardless of the mode of governance, unitary or dualist;
- we can see sometimes the equivalence of assignments of the Audit Committee with the assignments of the Management Board, being considered in general that the assignments of the Audit Committee are fulfilled by the Management Board;
- considering that the Audit Committee establishes relations with management, the Management Board, internal auditors, external auditors and with shareholders, it is necessary that the priority of the Audit Committee is to establish solid constructive relationships;
- we also observe the misunderstanding of the real role of the Audit Committee, which not only has the role of bringing to the knowledge of management the significant aspects acknowledged by the internal control, internal and external audit, but also actual monitoring of their activity;
- the Audit Committee must review and discuss with management and the financial auditors the financial statements of the entity and based on these discussions, to recommend their approval to the Management Board;
- the Audit Committee also has a consultative function regarding the strategy and policy of the company regarding the internal control system, the internal audit and the statutory audit;
- the Audit Committee must facilitate and encourage the communication between management, internal audit and external audit in order to promote a stronger corporate governance;
- the Audit Committee reports every year to the Management Board or the Supervisory Board

regarding the activity carried out during the previous year and whenever it considers appropriate or necessary for the fulfilment of its responsibilities;

- the public reporting by the Audit Committee regarding the independent evaluation of efficiency of internal control, internal audit, external audit and financial statements will have as consequence the enhancement of confidence of the public in the financial statements published;
- we cannot disregard the advantages of creation of an audit committee, among which we mention: reduction of risk of fraud by creation of a climate of discipline and control; the improvement of quality of financial reporting by own analysis of financial statements; consolidation of position of internal and external auditors, by the assurance of direct communication channels with management and the consolidation of the role of consultant of the Audit Committee.

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