

Strengthening the Audit Committee

Phil Kenkel

Bill Fitzwater Cooperative Chair

The purpose of the annual audit is to verify that the annual accounts provide a true and fair picture of the cooperative's finances. While some board members assume that one of the fundamental functions of the audit is to detect fraud, this is not the main aim of the audit. The audit is designed to detect material misstatements in the company's financial statements caused by either fraud or error. However the auditors only have a limited time in which to complete their work, so they concentrate on testing the validity of a sample of transactions. The cooperative could not afford for the audit team to examine every transaction. As someone once put it: "auditors and watchdogs, not bloodhounds".

Regardless of the actual purpose and limitations of the audit, cooperative members interpret the annual audit as a statement that the cooperative has a clean bill of health. A strong audit committee can help bridge the "expectation gap" between the member's view and what is possible from an external audit. While the auditor may have suggestions for improving internal controls, a strong audit committee examines that area proactively. As part of the audit planning process the audit committee should consider the cooperative's internal controls including issues such as: segregation of duties, rotation of duties, approved authority levels, spot checks and validation checks. Another area of internal controls is a whistleblower policy by which employees can report any suspected wrongdoing or inappropriate actions without fear of retaliation. Not only is it logical for the audit committee to develop and review the whistleblower policy, they can be a logical designated contact point since they are outside of the supervisory chain of command.

Another role for a strong audit committee is to examine the cooperative's financial ratios and benchmark the cooperative's performance against other similar cooperatives and industry standards. Members expect not only that the financial numbers are accurate (the role of the external auditor) but also that someone is considering whether those financial results are favorable.

The audit period might also be a good time to take a fresh look at cooperative's controls over physical assets. The CEO and staff probably have good procedures for securing inventories, equipment, facilities and buildings. Board members can still have unique perspectives on the weakest links in physical security and procedures through their daily interactions as customers. Information technology such as laptops, tablets, desktop computers and point of sales systems have become an increasingly important aspect of the cooperatives physical assets. Because of that, physical security measures also become a part of cyber security. I discuss some simple steps in cyber security in my next newsletter.

12-16-16