

The background of the top half of the page is a photograph of a business meeting. Several people are seated around a table, looking at documents and using laptops. The focus is on a person in the foreground who is writing on a document with a pen. The lighting is bright and professional.

AN OFFERING FROM THE BDO CENTER FOR CORPORATE
GOVERNANCE AND FINANCIAL REPORTING

Illustrative Audit Committee Charter

Audit committees that have the scope of their responsibilities (the “WHAT”) and how those responsibilities are carried out (the “HOW”) set forth in a written charter are more likely to play an effective role in overseeing a company’s financial reporting process. The following Illustrative Audit Committee Charter is intended as an example to assist the audit committee in constructing its own company-specific¹ charter that will be used as a working document or practical roadmap to outline its general and specific responsibilities and required duties. The charter should be assessed continually, but at least annually, to ensure that it captures and portrays the role of the audit committee accurately.

BDO has developed the following practice aid in conjunction with other BDO audit committee resources, including but not limited to the [Audit Committee Requirements Practice Aid](#), available within the [BDO Center for Corporate Governance and Financial Reporting](#), applicable exchange listing standards and SEC regulatory requirements, consideration of widely available audit committee charters and tools, and our knowledge and experience in working with both public company audit committees and those charged with governance at private companies.

Note: Throughout the example and embedded guidance, the terms “independent auditor(s)” and “external auditor(s)” are synonymous.

¹ In constructing its charter, the audit committee needs to consider the specific responsibilities and requirements of the audit committee as outlined under SEC rules as well as the Company’s respective listing exchange and should include consideration of additional facts and circumstances specific to the Company and consult with counsel and others, as necessary.

AUDIT COMMITTEE CHARTER REQUIREMENTS

Both the NYSE and NASDAQ require companies to have written audit committee charters. While the SEC does not require companies to adopt an audit committee charter, the SEC does require companies to disclose in their proxy statements whether the audit committee is governed by a charter, and if so, include a copy of the charter as an appendix to the proxy statement at least once every three years.

The following highlights the NYSE and NASDAQ minimum listing requirements for audit committee charters:

NYSE

NYSE (303A.07) requires the audit committee to have a written charter that addresses the committee's purpose. At a minimum, this must be to assist board oversight of:

- ▶ the integrity of the listed company's financial statements,
- ▶ the listed company's compliance with legal and regulatory requirements,
- ▶ the independent auditor's qualifications and independence, and
- ▶ the performance of the listed company's internal audit function² and independent auditors.

The charter must also address the audit committee's preparation of the corporate governance disclosures required by Item 407(d)(3)(i) of SEC Regulation S-K.

Additionally, the charter shall address the annual [performance](#) evaluation of the audit committee as well as the duties and responsibilities of the audit committee. Such responsibilities, at a minimum, must include those set out in [SEC Rule 10A-3\(b\)\(2\), \(3\), \(4\) and \(5\) of the 1934 Exchange Act](#)³ as well as the following:

- ▶ at least annually, obtain and review a report by the independent auditor describing: the firm's internal quality-control procedures; any material issues raised by the most recent internal quality-control review, or peer review, of the firm, or by any inquiry or investigation by governmental or professional authorities, within the preceding five years, respecting one or more independent audits carried out by the firm, and any steps taken to deal with any such issues; and (to assess the auditor's independence) all relationships between the independent auditor and the listed company;

- ▶ meet to review and discuss the Company's annual audited financial statements and quarterly financial statements with management and the independent auditor, including reviewing the Company's specific disclosures within MD&A;
- ▶ discuss the Company's earnings press releases, as well as financial information and earnings guidance provided to analysts and rating agencies;
- ▶ discuss policies with respect to risk assessment and risk management;
- ▶ meet separately, periodically, with management, with internal auditors (or other personnel responsible for the internal audit function) and with independent auditors;
- ▶ review with the independent auditor any audit problems or difficulties and management's response;
- ▶ set clear hiring policies for employees or former employees of the independent auditors; and
- ▶ report regularly to the board of directors.

NASDAQ

NASDAQ (IM-5605-3) requires each of its listed companies to adopt a formal written audit committee charter that specifies the scope of its responsibilities and the means by which it carries out those responsibilities; the external auditor's accountability to the audit committee; and the audit committee's responsibility to ensure the independence of the external auditor. Consistent with this, the charter must specify all audit committee responsibilities set forth in SEC Rule 10A-3(b)(2), (3), (4) and (5) under the 1934 Exchange Act.

Rule 5605(c)(3) imposes additional requirements for investment company audit committees that must also be set forth in audit committee charters for these companies.

² For NYSE listed companies, if the listed company does not yet have an internal audit function because it is availing itself of a transition period pursuant to Section 303A.00, the charter must provide that the committee will assist board oversight of the design and implementation of the internal audit function.

³ Under Rule 10A-3, these specifically pertain to the audit committee's responsibilities related to registered public accounting firms, complaints received by the company, the authority to engage advisors, and funding.

Note: Red font has been included throughout to prompt customization by users where appropriate.

Material discussed in this practice aid is meant to provide general information and should not be acted upon without first obtaining professional advice appropriately tailored to your individual circumstances.

[INSERT NAME OF COMPANY] AUDIT COMMITTEE CHARTER

This audit committee charter has been approved by the board of directors ("the board") of [insert Company name] ("the Company") on [insert date]. This charter shall guide the audit committee ("the committee") in fulfilling its governance responsibilities to the board in overseeing the integrity of the Company's accounting and financial reporting practices, policies, and processes and both the internal and external auditors.

Purpose

The committee is appointed by the board. The committee's role is to act on behalf of the board of directors and provide oversight of:

- ▶ The integrity of the Company's financial statements
- ▶ The Company's compliance with legal and regulatory requirements
- ▶ The independent auditor's qualifications and independence
- ▶ The performance of (if applicable) the Company's internal audit function and independent auditors

The committee's role includes a particular focus on the qualitative aspects of management's financial reporting to shareholders and on Company processes for the management of business/financial risk and for compliance with significant applicable legal, ethical and regulatory requirements. The role also includes coordination with other board committees and maintenance of strong, positive working relationships with management, external and internal auditors, counsel and other advisors.

(Consider including the following limitations. For example:) The committee is responsible for the duties set forth in this charter but is not responsible for either the preparation or the auditing of the financial statements. Management has the responsibility for preparing the financial statements and establishing and maintaining the appropriate related internal control environment. The external auditors are responsible to plan and perform an [integrated] audit to obtain reasonable assurance about whether management's financial statements are free of material misstatements, whether due to error or fraud. The external auditors are additionally responsible for assessing the effectiveness of the Company's internal controls over financial reporting, pursuant to the standards of the PCAOB.⁴

Composition

The committee shall consist of at least three independent (as defined by applicable listing standards), non-executive board members. Committee members shall have:

1. Knowledge of the primary industries in which the Company operates;
2. The ability to read and understand fundamental financial statements, including the Company's balance sheet, income statement, statement of cash flows and key performance indicators;
3. The ability to understand key business and financial risks and related controls and control processes.

⁴ If the external auditor is only engaged to perform an audit of financial statements only, modify to state: "The external auditors are responsible to plan and perform an audit to obtain reasonable assurance about whether management's financial statements are free of material misstatements, whether due to error or fraud."

The committee shall have access to its own counsel and other advisors at the committee's sole discretion. At least one member, preferably the chair, should be literate in business and financial reporting and control, including knowledge of the regulatory requirements, and should have past employment experience in finance or accounting or other comparable experience or background and shall be deemed "an audit committee financial expert."⁵ Committee appointments shall be approved annually by the full board upon recommendation of the nominating committee. The committee chairperson shall be selected by the committee members or by the nominating committee.

(If applicable, consider including restrictions as to the number and type of concurrent boards a member may serve. For example: The committee shall ensure each member has adequate time to devote to their duties. Committee members may not serve on more than [insert number] public company boards of directors unless the board has determined such service would not prevent members to effectively serve the Company.)

(If applicable, consider including any expectations as to tenure, termination, and resignation or any additional board refreshment policies, including mandatory retirement ages. For example: The committee member shall serve the committee until such time as the member's request to be removed from the committee, resignation from the board, or by removal from the board at the board's discretion.)

Committee Operating and Management Principles

The committee shall fulfill its oversight responsibilities within the context of the following overriding principles.

GENERAL RESPONSIBILITIES AND COMMUNICATIONS

The chair and others on the committee shall, to the extent appropriate, maintain an open avenue of contact throughout the year with senior management, other committee chairs and other key committee advisors (e.g., external and internal auditors, etc.), as applicable, to strengthen the committee's knowledge of relevant current and prospective business issues.

The committee shall have access to management without restriction and meet with management at least once per year separately.

ONBOARDING AND CONTINUING EDUCATION

The committee, with management, shall develop and provide appropriate and timely onboarding education and processes for new committee members. The committee shall participate in a process for review of important financial and operating topics that present potential significant risk to the Company. Additionally, individual committee members are encouraged to participate in relevant and appropriate continuing education to ensure understanding of the business and environment in which the Company operates as well as independence requirements of board members.

ANNUAL PLAN

The committee, with input from management and other key committee advisors, shall develop an annual plan responsive to the "primary committee responsibilities" detailed herein. The annual plan shall be reviewed and approved by the full board.

MEETINGS

Committee meeting agendas shall be the responsibility of the committee chair, with input from committee members. It is expected that the chair will also ask for management and key committee advisors, and perhaps others, to participate in this process.

The committee shall request members of management, counsel, internal and external auditors, as applicable, to participate in committee meetings, as necessary, to carry out the committee's responsibilities. Periodically, and at least annually, the committee shall meet in private sessions with only the committee members. It shall be understood that meetings between the committee and/or the committee chair with either internal or external auditors, or counsel, may, at any time, be deemed necessary, with or without management's attendance. In any case, the committee shall meet in executive sessions separately with internal and external auditors, at least annually.

The committee shall meet at least quarterly. Additional meetings shall be scheduled as considered necessary by the committee or chair. **(If applicable)** Meetings shall take place in person, telephonically, or by other means providing each member can actively participate.

⁵ As defined under applicable SEC rules.

EXPECTATIONS AND INFORMATION NEEDS

The committee shall communicate committee expectations and the nature, timing and extent of committee information needs to management, internal auditors and external parties, including external auditors. Written materials, including key performance indicators and measures related to key business and financial risks, shall be received from management, auditors and others at least one week in advance of meeting dates. Meeting conduct will assume committee members have reviewed written materials in sufficient depth to participate in committee/board dialogue.

EXTERNAL RESOURCES

The committee shall be authorized to access internal and external resources, as the committee requires, in carrying out its responsibilities. This includes the authority to hire and terminate internal and external auditors and advisors, as well as the responsibility to approve services and fees paid to such resources.

The committee shall have the authority to conduct or authorize investigations into any matter within the committee's scope of responsibilities. The committee will be empowered to retain independent counsel and other professionals to assist in conducting any investigation, who will report directly to the committee.

REPORTING

The committee, through the committee chair, shall report periodically, as deemed necessary, but at least semiannually, to the full board. In addition, summarized minutes from committee meetings, separately identifying monitoring activities from approvals, shall be available to each board member at least one week prior to the subsequent board of director's meeting.

The committee shall prepare an annual audit committee report to be included within the Company's annual proxy statement. The committee shall also disclose in the proxy statement that it is governed by a charter and include instructions on how to access the current charter.

The committee shall review and update the committee's charter at least annually.

SELF-ASSESSMENT

The committee shall review, discuss and assess its own performance as well as its role and responsibilities at least annually, seeking input from senior management, the full board and others. Changes in roles and/or responsibilities, if any, shall be recommended to the full board for approval.

Oversight of Risk Management and Financial Reporting Responsibilities

FINANCIAL REPORTING

The committee shall perform the following with respect to the Company's financial reporting:

- ▶ Discuss, review and assess the annual and interim financial statements, including earnings releases, with management and the auditors before they are released to the public or filed with the SEC and formally recommend to the board that the audited annual financial statements be included within the Company's annual report filed with the SEC.
- ▶ Discuss, review and assess the key financial statement issues and risks, their impact or potential effect on reported financial information, the processes used by management to address such matters, related auditors' views, and the basis for audit conclusions.
- ▶ Approve changes in important accounting principles and the application thereof in both interim and annual financial reports.
- ▶ Advise financial management and the auditors that they are expected to provide a timely analysis of significant current financial reporting issues and practices.
- ▶ (If applicable) Discuss and review management's use of non-generally accepted accounting principles ("non-GAAP") measures with the auditors.

RISKS AND CONTROLS

The committee shall perform the following with respect to the Company's risks and controls to address those risks:

- ▶ Review and assess the Company's business and financial risk management process, including the adequacy of the overall control environment and controls in selected areas representing significant risk.
- ▶ Review and assess the Company's system of internal controls for detecting accounting and financial reporting errors, fraud and defalcations, legal violations, and noncompliance with the corporate code of conduct. In that regard, review the related findings and recommendations of the external and internal auditors, together with management's responses.
- ▶ Review and discuss with the external auditor related parties, relationships or transactions with related parties and other significant unusual transactions.
- ▶ Review with legal counsel any regulatory matters that may have a material impact on the financial statements.
- ▶ Review the results of the annual audits of directors' and officers' expense accounts and management perquisites prepared by the internal auditors.
- ▶ **(If applicable⁶)** Review management's cybersecurity risk management program and its design and operating effectiveness with appropriate professionals, including but not limited to the Chief Information Officer, Chief Information Systems Officer, information technology staff, and external auditors.

Oversight of External and Internal Auditors

The committee shall perform the following with respect to its oversight of the external and internal auditors:

- ▶ Recommend the selection of the external auditors for approval by the board of directors and oversee the compensation of the external auditor.
- ▶ Review with the external auditor written required communications regarding their independence in accordance with Public Company Accounting Oversight Board (PCAOB) Independence Standards Board Standard No. 1.
- ▶ Monitor compliance with partner rotation and conflict of interest requirements.
- ▶ Instruct the external auditors that they are responsible to the board of directors and the committee as representatives of the shareholders. In that regard, confirm that the external auditors will report all relevant issues to the committee in response to agreed-upon expectations.
- ▶ Review, at least annually, the performance of the external and internal auditors.
- ▶ Obtain a formal written statement from the external auditors consistent with standards set by the PCAOB. Additionally, discuss with the auditors any relationships or nonaudit services that may affect their objectivity or independence.
- ▶ Consider, in consultation with the external and internal auditors, their audit scopes, overall audit strategy and timing of the audit to ensure completeness of coverage, reduction of redundant efforts and the effective use of audit resources.
- ▶ If applicable, discuss with the internal and external auditors the nature and extent of specialized skills or knowledge needed to address significant risks.
- ▶ If applicable, discuss with the internal and external auditors the extent to which there are plans to use the work of others and the basis for the external auditor's determination that he/she can serve as the principal auditor.
- ▶ Review and pre-approve requests for any audit-related or permitted non-audit services to be performed by the external auditors, and be advised of any other study undertaken at the request of management that is beyond the scope of the audit engagement letter.

⁶ In cases where cybersecurity is the responsibility of the full board, it may be a best practice to indicate within the audit committee charter.

- ▶ Review with management and the external auditors the results of the annual audit and related comments in consultation with other committees as deemed appropriate, including any key risk factors, difficulties or disputes with management, any significant changes in the audit plans, the rationale behind adoptions and changes in accounting principles, and accounting estimates requiring significant judgments.
- ▶ Provide a medium for the external auditors to discuss with the committee their judgments about the quality, not just the acceptability, of accounting principles and financial disclosure practices used or proposed to be adopted by the Company.
- ▶ Discuss the significant findings of the audit including:
 - Critical accounting policies and practices used by the Company;
 - Alternative accounting treatments within generally accepted accounting principles (GAAP) related to material items that have been discussed with management; and
 - Other material written communications between the accounting firm and management (e.g., management representation letters, engagement letters, etc.).
- ▶ Review with the external auditor the audit firm's quality control policies and procedures and any material issues raised by the most recent internal quality control review of the firm.
- ▶ Discuss with the external auditor PCAOB, other regulatory, and peer inspection findings and quality control measures.
- ▶ Review with the auditor the draft auditor's report on the annual audited financial statements.
- ▶ Approve changes in the directors of the internal audit function.
- ▶ Instruct the internal auditors that they are responsible to the board of directors through the committee.
- ▶ Review with the internal auditors any changes in the scope of their plans.
- ▶ Review with the internal auditors the results of their monitoring of compliance with the code of conduct.

Oversight of Compliance and Ethics

The committee shall perform the following with respect to its oversight of the compliance and ethics of the Company:

- ▶ Establish and monitor procedures for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters, including procedures for the confidential, anonymous submission by employees of the Company of concerns regarding questionable accounting or auditing matters.
- ▶ Review and approve all related party transactions.
- ▶ Review and update the Company's Code of Conduct ("the Code") and the Company's monitoring of compliance and enforcement of the Code.



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