

Audit Committees: The Last Best Hope

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The Letter adopts an Enterprise Risk Management (ERM) approach to specifically consider Executive Management Fraudulent Financial Reporting (EMFFR) in public companies. EMFFR is determined to be a catastrophic risk which demands enterprise attention. A simplified EMFFR risk model incorporates the “fraud triangle” into an enterprise perspective and offers an alternative approach to application of risk response interventions. Public company audit committees are presented as both owning EMFFR risk and as being “the party best placed to manage the risk response effectively.” Current influences on corporate governance within the U.S. are reviewed, management of EMFFR risk is recognized as a non-discretionary, non-delegatable function of the audit committee, and a structure for the audit committee to effectively manage EMFFR risk is introduced. The EMFFR risk management structure has three components: 1) forensic accountants as professional audit advisors to the audit committee; 2) use, by the audit committee, of the external auditor as a tool to obtain quality financial reporting from management through insistence upon neutral reporting; and, 3) forensic accountants embedded within the integrated internal controls/financial statement audit and focused exclusively upon active detection of EMFFR. A testable heuristic intended to improve the efficiency of peremptory EMFFR detection is offered.

(This Overview is not contained within the printed issue.)