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Banking and Capital Markets Industry Insights

2006 Audit Committee Survey Highlights

Executive Summary

2006 Audit Committee Survey for Banking and Capital Markets Firms



Since 2002, Ernst & Young has conducted a survey of audit committees of the largest, global financial institutions. This year, for the first time, the survey was expanded to include 11 additional industries.

Audit committee chairs, audit committee members, board members, and others from 176 companies participated – 47 of them from banks and capital markets firms.

The role of the audit committee always has been to ensure the quality and integrity of the company's audit and related accounting and reporting practices. Thanks to mandates like Sarbanes-Oxley, today the audit committee's role also encompasses the broad issue of risk management and its potential implications on the financial health of the company. And when it comes to effective risk governance, audit committees of banks are at the forefront of leading practices. That's just one of the major findings of Ernst & Young's fourth annual Audit Committee Survey.

In years past, the survey has focused solely on audit committees at banks and capital markets firms. This year, in order to gain a better understanding of audit committee practices overall, Ernst & Young expanded the survey to 11 industries including asset management, consumer products, insurance, media and entertainment, oil and gas, pharmaceuticals and biotechnology, technology, telecommunications, real estate, and utilities.

Executive Summary

2006 Audit Committee Survey for Banking and Capital Markets Firms



To view results for audit committees across all industries surveyed, please visit:

www.eyonline.com/auditcommittee

Although the survey indicates that banks and capital markets firms are leading the way in risk governance, audit committees in both banking and other industries report being faced with the same monumental challenge: consolidating risk efforts into a coordinated process. This task is especially challenging for banks as they are more likely to have complex regulatory processes. If banks continue to serve as a model for other industries, it is probable that they will be the first industry to converge their risk and compliance activities into a process that offers more effective risk management for the entire enterprise.

We hope these observations provide useful insights about the overall trends of audit committees and the ways in which banking and capital markets fare against other industries. The results also may be useful as a basis to compare an individual institution's responses to those of other institutions.

We welcome your comments and observations.

Table of Contents

Industry Comparison – page 4

Overview – page 6

Risk Management – page 7

Audit Committee Activities – page 9

Audit Committee Composition, Education, and Orientation – page 10

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Industry Comparison

Key Observations



When comparing the banking and capital markets industry to all other industries surveyed, there are some key differences in the area of risk management.

- The majority of banking audit committees report that managing various risk issues is part of their primary responsibilities: regulatory, Sarbanes-Oxley, anti-money laundering/U.S. Patriot Act, compliance systems and processes, and disaster risks. They also report that they have a comprehensive process and structure to identify and manage risks; 94% in comparison to 72% of non-bank respondents.
- Given the prominence of risk management in banking, it is not unexpected to find that the banking and capital markets industry has a better understanding of the breadth of issues facing their companies. As such, their audit committees include meeting with regulators as one of the committee's key activities; 62% vs. 8% in other industries.
- Regulatory risk is among the top three risk issues, followed by market dynamics, and M&A and divestiture, for audit committees in all industries except banking and capital markets. The top three risk issues for banks were reputation, IT, and credit. Interestingly, all industries cited people/HR as one of their top five risk issues.
- Despite an increased focus on risk, only 9% of boards have a separate risk committee, whereas 54% of boards at banking and capital markets firms have a risk committee.

Industry Comparison

Key Observations



Bank audit committees invest significantly more time, resources, and education than do other audit committees.

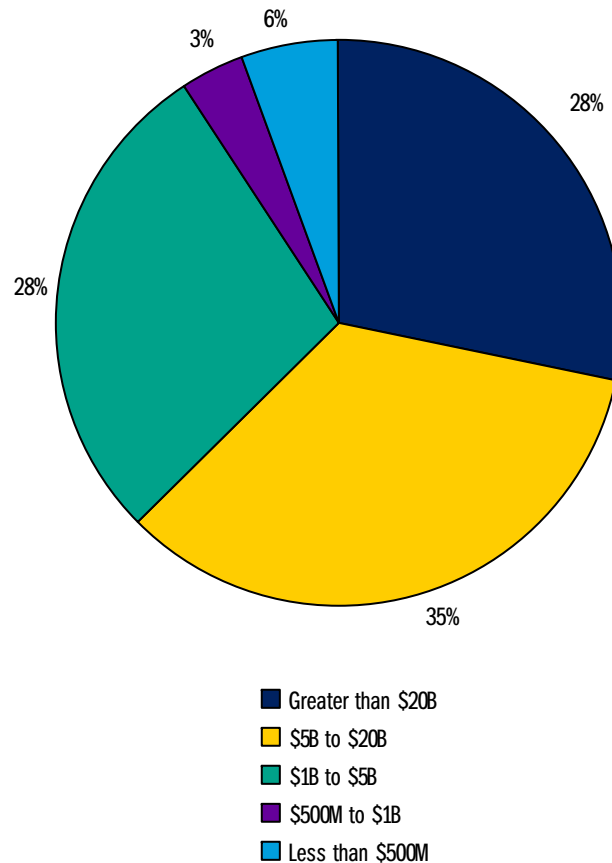
- Bank audit committees have more financial experts than do audit committees in non-banking industries. They are also more likely to consider various areas of expertise, such as executive/CEO and industry experience, when recruiting new members. Conversely, the majority of non-bank audit committees indicate that they are most likely to seek financial experts when recruiting new members.
- Although approximately two-thirds of audit committees have primary governance responsibility for regulatory risk, no respondents – across all industries – indicate that they look for new members with legal or regulatory experience.
- In terms of continuing education, 50% of banks have a formal process in place, while only 37% of other industries do. Bank audit committees are also more likely to have orientation programs, hold more meetings, spend more hours on average annually fulfilling their duties, and receive higher compensation.

Overview

Annual Revenues



Annual Revenues of All Companies Surveyed



- 47 banking and capital markets companies participated.
- 63% of respondents have revenues greater than U.S. \$5 billion and 62% have more than 10,000 employees.
- U.S.-based companies make up 61% of the respondents, 23% are European-based companies, and the remaining 16% are based in countries outside of the U.S. and Europe.
- More than 30 global stock exchanges are represented.

Risk Management

Key Observations for Banking and Capital Markets Firms



- The majority of respondents indicate the risks most frequently delegated to the audit committee are:
 - Accounting and reporting issues
 - Capital structure
 - Sarbanes-Oxley
 - Tax exposure
 - Regulatory
 - Compliance systems
 - U.S. Patriot Act
 - Other regulatory compliance risk.
- Accounting and reporting is the area most frequently delegated to the audit committee, yet this is the second most common risk area where the audit committee believes more education is necessary.
- Almost all (93%) respondents indicate that their company has a comprehensive process and structure in place to identify and manage risks specifically related to its business strategies and objectives.

Risk Management

Key Observations for Banking and Capital Markets Firms



- Additionally, all respondents indicate that the company has a clear understanding of its risk profile from strategic, operational, financial, and compliance perspectives.
- Two-thirds (67%) of respondents indicate that company management provides the audit committee with risk-related information – such as a “risk dashboard” – on a quarterly basis.
- About 13% of respondents indicate that the company provides the audit committee with risk updates monthly or more frequently.
- Respondents also include the following as the most important challenges facing the company in risk management:
 - Responding to market risks in a timely manner
 - Consolidating risk efforts into a coordinated process
 - Identifying and classifying new potential risks that are unique to subsidiaries.

Audit Committee Activities

Key Observations for Banking and Capital Markets Firms



- Audit committees typically hold four to seven full agenda meetings a year. Most are held on a quarterly or bi-monthly basis.
- Approximately 40% of audit committees hold between one and four specific scope meetings per year; 57% of audit committees do not hold special/ad hoc meetings.
- The average length of full agenda meetings for audit committees is 4.3 hours; the average length of specific scope meetings for audit committees is 1.6 hours.
- The average audit committee member spent 141 hours, over the course of 12 months, on committee activities. Of the 141 hours, 43 hours were spent attending board meetings.
- On average, audit committees spend 44% of meeting time reviewing/discussing presentations that were previously provided by management, internal audit, and external audit. Only 34% of their time is devoted to discussion and Q&A on previously provided materials. Another 10% of their time is spent discussing materials not previously provided.

Audit Committee Composition, Education, and Orientation

Key Observations for Banking and Capital Markets Firms



- The majority of respondents indicate that more education for the audit committee is needed for the following risk areas:
 - IT
 - Accounting and reporting
 - Basel II implementation.
- 91% of audit committees have an orientation program; 50% have a formal education process in place.
- 25% of audit committees look for new members that have executive/CEO experience.
- For those reporting income in both years, compensation for audit committee members is approximately 15% higher in 2006 compared to 2005. The median annual additional compensation for the audit committee chair was U.S. \$19,000.

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