



Audit Committee  
effectiveness

2020 Framework



MAKING AN  
IMPACT THAT  
MATTERS  
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# Introductory letter

Dear Audit Committee Member,

Given how rapidly expectations of the audit committee are changing, there is one question every audit committee member wants to know – are we covering the ground well? We are often asked for an independent view of how the audit committee is performing, and to help with this we drew up our Audit Committee effectiveness framework, which we first published in 2015. It is striking just how far the audit committee's agenda has grown in the five years since.

The work of the audit committee has never been more important: investors, other stakeholders and regulators demand ever more informative and reliable reporting, not just of the results and financial position, but of strategy, resilience, long term value creation, of values, of a company's role in climate change, not to mention the community and the whole public interest agenda. The audit committee plays a prominent role in establishing and maintaining "deserved confidence" in a company, with specific independent endorsement by auditors in certain areas.

The implementation of many of the recommendations put forward in the Competition and Markets Authority (CMA), Kingman and Brydon reviews to enhance corporate reporting and audit in the UK will impact the audit committee considerably. The Brydon review draws out the public interest aspects of reporting and audit, proposing new statements in which the audit committee will have a particular interest: a Public Interest Statement and a Resilience Statement. Brydon also proposes that a company should consult with shareholders on its articulation and management of risks and on the company's Audit and Assurance Policy<sup>1</sup>. Both Kingman and Brydon supported the introduction of a more formal internal control regime for the largest UK listed companies, and consultations on the implementation of these are expected in the UK during 2021. Furthermore, the Financial Reporting Council's (FRC) future oversight of company reporting will include the whole of the annual report from 2021 and it is likely that the FRC's supervision powers will cover all directors even where they are not an accountant. Dialogue within and supervision of the reporting ecosystem is at last recognising where the responsibilities lie.

To assist with the annual Code requirement to review the effectiveness of your audit committee, committee members will want to keep current with the range of new calls on their time and attention. Given how much the landscape has already changed for audit committees, we decided to update this effectiveness framework for current expectations, even though more changes will emanate from the 2021 consultations on corporate reporting and audit reform. Indeed, the FRC is itself suggesting the need to develop a set of minimum standard expectations for the audit committee. In this edition, we label clearly what is "direction of travel" and what is new "in issue" materials since the last edition: the 2018 UK Corporate Governance Code; the new Internal Audit Code of Practice; the FRC's revised Ethical Standard 2019; updated standards on auditing; and the Financial Conduct Authority's (FCA) consultation on mandatory climate-related disclosures. These in themselves represent more ground to cover for most audit committees – reinforcing that even the best committees require the support of a well informed and well organised secretary.

We trust you will find this framework helpful, and we would be very interested to hear your feedback. If you believe your evaluation could benefit from professional external facilitation, you know where to find us.

Finally, don't forget that you and your colleagues can join us at the Deloitte Academy where we host live updates to air current issues and enable you to swap notes with your peers.

Yours faithfully,



**William Touche**  
Vice Chair

<sup>1</sup> Deloitte's publication [Developing your company's Audit and Assurance Policy](#) is a helpful resource in this area, and includes a framework for developing and reviewing internal controls over financial reporting.



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# About this framework

This practical self assessment guide covers all aspects of the audit committee's remit for companies outside the financial sector. Regulatory requirements are drawn from the [UK Corporate Governance Code](#), the FRC's Guidance on [Audit Committees](#), the FRC's [Guidance on Risk Management](#), Internal Control and Related Financial and Business Reporting, the FRC's revised [Ethical Standard 2019](#) and the [CMA's final order](#). It also includes new materials: the new [Internal Audit Code of Practice](#), and the FCA's consultation on mandatory climate-related disclosures aligned to the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD).

As well as covering all the mandated areas, we have added some key considerations around narrative reporting, particularly relevant in the current volatile economic environment. We also reflect in this framework areas where we expect the audit committee to have an increasing role in future and have incorporated questions on climate change, on audit and assurance policies and on wider stakeholders. To be clear, however, the framework does not anticipate the results of any future consultations on changes to the board or audit committee remit, auditor responsibilities or corporate reporting, but does take into account areas where expansion of role can be expected.

As in previous editions, we have included a number of qualitative considerations in the form of 'good practice statements' which help to differentiate an effective audit committee from one which is just ticking the boxes.



# How to use this framework

Inevitably perhaps, reflecting the complexities of modern business life, this is a long framework. Audit committees will not want or need to answer all of the questions on an annual basis. Instead, we recommend covering the different sections on a rotation basis. The framework is structured to allow you to focus on the requirements of the Code or other regulation and then decide which areas of the audit committee's structure and remit merit a deeper dive into guidance and qualitative considerations.

To facilitate that decision, each section is broken down into three parts:

- **Requirements** – these come directly from law, the UK Corporate Governance Code or requirements with similar importance – we would expect these to be assessed annually, to assess compliance.
- **Guidance** – it is also advisable to follow the guidance, which is usually issued by the FRC, the Chartered Institute of Internal Auditors (IIA) or similar bodies.
- **Qualitative considerations** – these are suggested best practice considerations developed by our specialists to identify areas where audit committees can recognise their own leading practices and incorporate those used by other leading audit committees.

Some audit committees may wish to add one or more of the “deep dive” sections – covering stakeholders, climate, cyber and data security – to assess their existing span of activities.

For each statement, respondents should decide whether this is an area for further focus, an area where the committee is performing as expected, or a special strength. This can be typed or written next to the statement, allowing responses to be retained and compared for discussion. The section Finalising your self- assessment can then be used to summarise the scores you have given and your key observations.



# Setting up for success



# A. Establishment, membership and appointment

While all board directors have a duty to act in the interests of the company the audit committee has a particular role, acting independently from the executive, to ensure that the interests of shareholders are properly protected in relation to financial reporting and the risk management and internal control over that reporting.

Appointments to the audit committee should be made by the board on the recommendation of the nomination committee, in consultation with the audit committee chair.

In considering the composition of the audit committee, the nominations committee and board should consider the range of skills, experience, knowledge and professional qualifications of current and proposed committee members. There are some limited requirements under the Code and the need for a degree of financial literacy among the other members will vary according to the nature of the company. However, experience of corporate financial matters will normally be required.

Formal requirements in this area are driven by the Code, the Disclosure & Transparency Rules (DTR) and the Guidance.

Code provision		Rating 1,2 or 3
A1	The audit committee has at least three, or in the case of smaller companies two, members (24).	
A2	The audit committee members are all independent under provision B.1.1 of the Code (24).	
A3	At least one member of the audit committee has recent and relevant financial experience (24). N.B. The Disclosure & Transparency Rules (DTR) require that at least one member must have competence in accounting or auditing, or both (DTR 7.1.1A); and this requirement may be satisfied by the same member or by different members (DTR 7.1.2).	
A4	The audit committee as a whole has competence relevant to the sector in which the company operates (24).	
Guidance on audit committees		Rating 1,2 or 3
A5	Appointments to the audit committee are made by the board on the recommendation of the nomination committee, in consultation with the audit committee chair (13).	
A6	The level of remuneration paid to members of the audit committee takes into account the level of fees paid to other members of the board. The remuneration of the audit committee chair reflects the heavier responsibilities and time demands of this role (28).	
Guidance on board effectiveness		Rating 1,2 or 3
A7	The chair should ensure that committee membership is periodically refreshed and that individual independent non-executive directors are not over-burdened when deciding the chairs and membership of committees (63).	
Qualitative considerations		Rating 1,2 or 3
A8	The audit committee is sufficiently diverse to avoid the risk of "groupthink".	
A9	There is a clear succession plan in place for future membership of the audit committee, allowing the nomination committee adequate time to consider appropriate replacements.	

**Total of ratings**

**Comments:**





## B. The audit committee chair

The audit committee chair sets the tone for and leads the audit committee. For this the chair will develop a deep understanding of the company and its industry, the regulatory context and technical accounting and reporting issues. Chairing the committee will involve leading discussions with (and challenge of) members of the executive, the internal auditor and the external auditor.

The chair should communicate clearly with the board, seek views from committee members, and be proactive about engagement with shareholders at the annual general meeting and other occasions.

There are no specific requirements in relation to the role of the audit committee chair. The assessment in this area is driven by the FRC's Guidance on audit committees and some qualitative considerations.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

Guidance on audit committees		Rating 1,2 or 3
B1	The audit committee chair keeps in touch on a continuing basis with the key people involved in the company's governance, including the board chair, the chief executive, the finance director, the external audit lead partner and the head of internal audit (22).	
Qualitative considerations		Rating 1,2 or 3
B2	The committee chair is demonstrably committed to the integrity of all aspects of corporate reporting (both in the annual report and on the company website), internal control, risk management and audit quality.	
B3	The audit committee chair inspires confidence. The audit committee members value the chair's opinion and believe that the chair demonstrates clear leadership of the committee and acts as a driving force within the committee to ensure all audit committee members are contributing effectively.	
B4	The audit committee chair brings an independent perspective and challenge when it comes to management, the internal auditor and the external auditor.	
B5	The audit committee chair performs their role with enthusiasm, acts as a catalyst for change and brings ideas and insights to help the organisation to be more successful.	
B6	The audit committee chair has the confidence of shareholders and is proactive about seeking meetings with shareholders to seek input about significant matters within the remit of the committee.	

**Total of ratings**

**Comments:**



## C. Skills, experience, training and mindset

Audit committee members should bring expertise and experience to the role, which may include recent and relevant financial experience. Each committee member should have sufficient financial and risk management literacy to be able to identify and raise any concerns about internal controls, accounting judgements and reporting obligations. Additional skills in areas that are relevant to the company's industry sector or particular risk profile are valuable.

Structured ongoing training should be provided for the committee as a whole and for each member as required. Internal or external experts are often invited to offer training on specialist areas within the remit of the audit committee that are current regulatory or governance areas of focus.

There are no specific requirements in relation to skills, experience, training and mindset for the audit committee, other than those already laid out in Section A. The assessment in this area is driven by the FRC's Guidance on audit committees and some qualitative considerations

Requirements		Guidance	Qualitative considerations	1 Area for focus	2 Performing as expected	3 Special strength
<b>Guidance on audit committees</b>						<b>Rating 1,2 or 3</b>
C1	The committee members bring an independent mindset to their role (14).					
C2	Members have a degree of financial literacy and experience of corporate financial matters (15).					
C3	An induction programme is provided for new audit committee members, covering the role of the audit committee, its terms of reference, expected time commitment and an overview of the company's business model and strategy, identifying the main business and financial dynamics and risks. It could also include meeting some of the company staff (16).					
C4	Training is provided on an ongoing and timely basis and includes an understanding of the principles of and developments in corporate reporting and regulation (17).					
<b>Qualitative considerations</b>						<b>Rating 1,2 or 3</b>
The ongoing training requirements of committee members are agreed at the start of each year according to their specific needs and current industry context. Topics should be determined for training deep dives such as:						
<ul style="list-style-type: none"> <li>• Changing technology/digital landscape</li> <li>• Incorporation of automation and AI into operations</li> </ul>						
C5	<ul style="list-style-type: none"> <li>• Emerging business model risks such as developments in international trade agreements, climate change, response to pandemics</li> <li>• Supply chain resilience – including understanding of both outsourced and insourced partners</li> </ul>					
<i>NB This understanding should be sufficient to identify related risks and opportunities and determine areas where any further assurance may be required.</i>						
C6	Each committee member, as should all board members, bears in mind and promotes discussion of the directors' duties under s172, ensuring consideration of long term consequences of decisions, the interests of stakeholders, communities and the environment, company reputation and the need to act fairly between shareholders.					

**Total of ratings**

**Comments:**



## D. Meetings of the committee

The committee should meet as many times as it considers necessary to meet its responsibilities under its terms of reference. Currently, audit committees outside financial services are meeting 4-5 times per year. Meetings are usually aligned to the financial reporting and external audit cycle.

Where the audit committee also acts as a risk committee, further meetings may be required to ensure that adequate focus can be given to risk management and internal controls as well as the financial reporting cycle.

There are no specific requirements in relation to meetings of the committee. The assessment in this area is driven by the FRC's Guidance on audit committees and some qualitative considerations.

■ Requirements ■ Guidance ■ Qualitative considerations

1 Area for focus 2 Performing as expected 3 Special strength

Guidance on audit committees		Rating 1,2 or 3
D1	The number of audit committee meetings is sufficient to meet the audit committee's role and responsibilities, is not fewer than three per year and the meetings are held to coincide with key dates within the financial reporting and audit cycle. For example, when the audit plans (internal and external) are available for review and when interim statements, preliminary announcements and the full annual report are near completion (18).	
D2	No one other than the audit committee chair and members receive automatic invitations to a meeting of the audit committee. The external audit partner, the finance director and head of internal audit are invited to attend on a regular basis (20).	
D3	There is sufficient time between audit committee meetings and main board meetings to allow any work arising from the audit committee meeting to be carried out and reported to the board as appropriate (19).	
D4	At least once a year the audit committee meets the external and internal auditors without management present (21).	
Qualitative considerations		Rating 1,2 or 3
D5	The committee's agenda is set in a timely manner and circulated well in advance of meetings to all members and other invited attendees with appropriate supporting papers.	
D6	There is a clear plan for the year to ensure that all matters falling within the remit of the audit committee are covered over the year.	
D7	Items on the agenda are set with consideration of regulatory requirements, the company's reporting timetable and after considering key issues identified by management, the chief risk officer, the director of internal audit and the external auditors; and, where applicable, the input sought from stakeholders such as shareholders or employees.	
D8	The agenda gives appropriate focus on the most important issues, key judgements, and risk areas, ensuring that the committee's focus is spent on the most critical areas.	
D9	The meeting cycle allows time for "deep dives" in areas of particular complexity or interest, and for proper audit committee review of investigations.	
D10	Meetings of the committee are of an appropriate length and ensure that all key agenda items are well considered, and allow each member the opportunity to raise any queries or areas for discussion.	

**Total of ratings**

**Comments:**



## E. Support and resources

The audit committee should be able to rely on the company secretary in managing agendas and papers and for practical assistance and support. However, it is for the audit committee to determine what other resources it requires to properly fulfil its remit. This could include access to external legal or other professional advice in specialist areas.

There are no specific requirements in relation to support and resources. The assessment in this area is driven by the FRC’s Guidance on audit committees and some qualitative considerations.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

Guidance on audit committees		Rating 1,2 or 3
E1	The audit committee is provided with sufficient resources to undertake its duties (23).	
E2	The audit committee has access to the services of the company secretariat on all audit committee matters including: assisting the chair in planning the audit committee’s work, drawing up meeting agendas, taking minutes, drafting of material about its activities for the annual report, collection and distribution of information and provision of any necessary practical support (24).	
E3	The company secretary ensures that the audit committee receives information and papers in a timely manner to enable full and proper consideration to be given to the issues (25).	
E4	The board makes funds available to the audit committee to enable it to take independent legal, accounting or other advice when the audit committee reasonably believes it necessary to do so (26).	
Qualitative considerations		Rating 1,2 or 3
E5	The audit committee assesses its confidence in the quality of the management information provided to it - from the finance function covering accounting and tax issues and judgements and, from other parts of the company, covering ethical and conduct matters, workforce information and compliance with laws and regulations. Where necessary the committee plans for additional assurance (see section G).	

**Total of ratings**

**Comments:**



## F. Relationship with the board

The audit committee should report back to the board on a regular basis, usually as a standing board agenda item delivered by the chair of the audit committee. All board members of course have access to committee papers and may request to attend as an observer at the audit committee.

The chair of the board and respective committee chairs, should work with the executive to ensure there is clarity between the roles and remit of the audit committee and other committees, such as the risk committee, the sustainability committee or the disclosure committee.

There are no specific requirements in relation to the relationship with the board. The assessment in this area is driven by the FRC's Guidance on audit committees and Guidance on board effectiveness, with some qualitative considerations.

Requirements		Guidance		Qualitative considerations		1 Area for focus	2 Performing as expected	3 Special strength	
<b>Guidance on audit committees</b>								<b>Rating 1,2 or 3</b>	
F1	The main role and responsibilities of the audit committee are set out in written terms of reference tailored to the particular circumstances of the company (10).								
F2	The audit committee and board reviews the effectiveness of the audit committee on an annual basis (11).								
F3	Disagreements between the audit committee and the board are given adequate time for discussion. The audit committee has the right to report unresolved issues to shareholders as part of the report on its activities in the annual report (30).								
F4	The audit committee discusses what information and assurance it requires in order to properly carry out its role to review, monitor and provide assurance or recommendations to the board and, where there are gaps, how these should be addressed. The audit committee satisfies itself that these sources of assurance and information are sufficient and objective (31).								
<b>Guidance on board effectiveness</b>								<b>Rating 1,2 or 3</b>	
F5	The chair should ensure that sufficient time is allowed at the board for committees to report on the nature and content of discussion, on recommendations, and on actions to be taken (62).								
F6	The minutes of committee meetings should be circulated to all board members and the company secretary, unless, exceptionally, it would be inappropriate to do so (65).								
F7	The remit of each committee, and the processes of interaction between committees and between each committee and the board, should be reviewed regularly, for example, during the board evaluation (65).								
<b>Qualitative considerations</b>								<b>Rating 1,2 or 3</b>	
F8	The audit committee has time allotted annually to review the terms of reference, to ensure they remain current and in line with expectations and industry peers.								
F9	The audit committee and board have established clear criteria for assessing the effectiveness of the audit committee to inform their annual assessment of board and audit committee effectiveness.								

**Total of ratings**

**Comments:**



# G. Establishing an audit and assurance policy

Whilst the terms of reference of the committee establishes its overall remit, the audit committee should document its scope, activities and approach in a further level of detail to inject greater clarity around the role of the audit committee.

To assist with this, and to encourage stakeholder alignment, in his report published in December 2019, Sir Donald Brydon introduced the concept that companies should establish and publish an “Audit and Assurance Policy”. This would make clearer the extent of all assurance, addressing the “audit universe” of internal and external audit as well as additional assurance activity often undertaken by specialists, over areas such as cyber risk or climate impacts. It would also indicate the relationship to risks identified by the audit committee as part of its remit to understand principal and emerging risks and the related controls.

Although currently there is no requirement for an audit committee to establish such a policy, it seems clear that this is a sensible codification of audit committee assurance considerations and therefore all audit committees should be encouraged to develop one, whether they choose to publish it or not. Brydon proposes that the policy should be published on a three year “rolling” basis to be approved annually at the AGM. According to Brydon, this would provide an opportunity for audit committees to show how they are assuring the integrity of reporting and handling of risk, whether required to do so by law or not. The rolling nature of the policy would make it simple to reflect changes in circumstances and to evidence learning.

The policy would include an assurance budget split between external audit, internal audit and other forms of assurance. It would also:

- Explain the process of appointing auditors, the work demanded of them and the fees basis for audit work;
- Provide a framework for decisions about materiality;
- Explain how seeking assurance relates to the principal and emerging risks identified by the directors;
- Indicate how shareholders should interpret the resulting audit reports;
- Explain the approach taken to compiling the Resilience Statement (see section N) and the extent of assurance on this; and
- Explain the approach taken to obtaining and reporting on assurance around internal controls, both in relation to the financial reporting and operational controls; and
- Explain the approach taken to obtaining and reporting on assurance around other elements of the annual report.

Where there is a separate risk committee, audit committees may wish to skip or answer “not applicable” to some of these questions.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

Qualitative considerations	Rating 1,2 or 3
G1 The audit committee considers the principal and emerging risks to the business and both its financial reporting and operational controls, and identifies any areas where additional audit or assurance coverage would be of benefit, for instance corporate culture, alternative performance measures, key performance indicators. The committee establishes a policy regarding which of these areas should be covered by internal or external auditors or other providers of assurance and how frequently that should happen.	
G2 The audit committee determines its framework for decisions about materiality and is able to articulate this to stakeholders	
G3 The audit committee considers whether any form of assurance should be obtained over specific information conveyed in the annual report by the directors, in particular: <ul style="list-style-type: none"> <li>• The confirmation that information in the strategic report is “fair, balanced and understandable” and that it contains sufficient information to understand the position, performance, strategy and business model of the company.</li> <li>• The disclosures in the front half of the annual report regarding corporate purpose, whether it is clearly articulated and linked to the company’s strategy and values, and the explanation of how purpose, strategy and values align with the company’s culture.</li> <li>• The s172(1) statement, explanations of engagement with stakeholders and input obtained.</li> <li>• Key performance indicators, especially where KPIs and other metrics are of interest to investors.</li> </ul>	



# G. Establishing an audit and assurance policy

■ Requirements 
 ■ Guidance 
 ■ Qualitative considerations

**1** Area for focus    **2** Performing as expected    **3** Special strength

Qualitative considerations	Rating 1,2 or 3
G4    The audit committee assesses whether there are significant corporate events or activities planned where assurance would provide benefits – such as changes in systems or control environment, new accounting judgements, acquisitions, new businesses being launched, outsourcing, planned divestments.	
G5    The audit committee has considered the level of assurance over other information published by the company, such as: <ul style="list-style-type: none"> <li>• Interim financial statements</li> <li>• Updates to the market</li> <li>• Presentations to analysts</li> <li>• Information provided to regulators</li> <li>• Other information, such as Gender and Ethnicity Pay Gap, Prompt Payment practices, Modern Slavery Statements</li> </ul>	
G6    The audit committee considers whether input should be obtained from stakeholders such as shareholders or employees on its audit and assurance policy and if so puts in place procedures for this.	

**Total of ratings**

**Comments:**



# The audit committee agenda





# H. Oversight of accounting judgements, business and financial reporting and other company announcements

Under the Code, the audit committee is responsible for monitoring the integrity of the financial statements of the company and any formal announcements relating to the company's financial performance and for reviewing any related significant financial reporting judgements.

In particular, the audit committee determines which financial reporting matters and judgements are significant in each reporting period and challenges the conclusions on these. The audit committee should also understand how pervasive forecasting is to the financial statements, consider the historical accuracy of forecasting and be persuaded that judgements that rely on forecasts are sound.

In the UK, government transparency requirements have led to some public interest reporting outside the annual report – for instance, gender pay gap and reporting on payment practices and performance. Some companies are additionally reporting their ethnicity pay gap and certain sustainability data. The audit committee should consider how much oversight of these other forms of external reporting should be exercised in order to ensure focus, accuracy and consistency with other external announcements.

Formal requirements in this area are driven by the Code, the DTR and the Guidance, with public interest reporting requirements driven by separate regulation.

■ Requirements
 ■ Guidance
 ■ Qualitative considerations

1 Area for focus
 2 Performing as expected
 3 Special strength

Code provision	Rating 1,2 or 3
H1 The audit committee monitors the integrity of the financial statements of the company and any formal announcements relating to the company's financial performance and reviews significant financial reporting judgements (25).	
H2 Where requested by the board, the audit committee provides advice on whether the annual report and accounts taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy (25).	
Guidance on audit committees	Rating 1,2 or 3
H3 The audit committee considers key matters of their own initiative rather than relying solely on the work of the external auditor (31).	
H4 The audit committee reviews, and reports to the board on, the significant financial reporting issues and judgements made in connection with the preparation of the company's financial statements, interim reports, preliminary announcements and related formal statements (32).	
H5 The audit committee considers significant accounting policies and any changes to them (33).	
H6 The audit committee reviews the clarity and completeness of disclosures in the financial statements and considers whether the disclosures made are set properly in context (34).	
H7 If the audit committee is not satisfied with any aspect of the proposed financial reporting by the company, it reports its views to the board (35).	
H8 The audit committee reviews related information presented with the financial statements, including the strategic report, and corporate governance statements relating to the audit and to risk management (36).	



# H. Oversight of accounting judgements, business and financial reporting and other company announcements

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

H9	Whenever practicable, statements made by the company containing financial information are reviewed by the audit committee before board approval is given (38).	
H10	When advising the board on making the 'fair, balanced and understandable' statement, the audit committee assesses whether other information presented in the annual report is consistent with the financial statements (37).	
<b>Qualitative considerations</b>		<b>Rating 1,2 or 3</b>
H11	The audit committee understands the pervasive nature of management forecasts both for the significant judgements affecting financial reporting and the assessment of longer term viability and is satisfied that the forecasting process is robust.	
H12	The audit committee asks management to explain the reason that misstatements have been identified and requests that all adjustments are booked.	
H13	The audit committee asks management to consider alternative accounting treatments highlighted by the auditors, to explain the reason for any significant disclosure omissions reported by the auditors and where the audit committee agrees these are significant requests that amendments are made to the annual report.	
H14	The audit committee considers the disclosures in the front half of the annual report regarding corporate purpose, whether it is clearly articulated and linked to the company's strategy and values, and whether the annual report explains how purpose, strategy and values align with the company's culture.	
H15	The audit committee reviews any material related-party transactions prior to their consummation and considers the company's obligations under relevant disclosure requirements.	
H16	The audit committee is informed of and where requested has prompt sight of reports from third party advisers on legal issues (actual or potential), tax matters, accounting and valuation matters and reports from regulators.	
H17	The audit committee reviews all earnings press releases and the financial information and earnings guidance provided to analysts and ratings agencies and recommends their release to the board.	
H18	The audit committee reviews all other external information published by the company to meet or anticipate regulatory requirements, for example on sustainability, tax strategy, modern slavery, gender pay gap, ethnicity pay gap and payment practices and performance reporting, has the opportunity to ask questions about the composition and consistency of the information and to request amendments where necessary.	
H19	The audit committee has considered and is satisfied with the company's tax strategy, state of tax compliance and the reporting of tax arrangements to shareholders and others.	



# H. Oversight of accounting judgements, business and financial reporting and other company announcements

■ Requirements ■ Guidance ■ Qualitative considerations

1 Area for focus 2 Performing as expected 3 Special strength

H20 When requested by the board to review the annual report to determine whether it is fair, balanced and understandable, the audit committee requests and considers suitable supporting material, for example a report that lists items that have gone well balanced against those that have not gone so well during the period, so that the audit committee can assess whether the balance is appropriate.

H21 When reviewing the annual report and other company announcements, the audit committee considers the quality of reporting on current hot topics, such as the following:

- **Regulatory areas of focus** – have the most recent observations on corporate reporting, risk reporting, accounting, corporate governance from the FRC, FCA, and other relevant regulators been taken into account?
- **Areas of focus for investors** – is the audit committee satisfied with its process for determining areas of current investor attention? Have the most significant areas of focus for major investors been taken into account when determining how best to communicate the company's position, performance, business model and strategy?
- **COVID-19** – have the forecasting judgements, any viability implications, effect on strategy or business model and other stakeholder information needs when reporting in times of uncertainty been adequately disclosed?
- **Climate** – have the forecasting judgements, any viability implications, effect on strategy or business model and other stakeholder information needs when reporting in times of uncertainty been adequately disclosed?
- **International trade** – have the consequential risks and uncertainties in the international political and trading environment been adequately reflected?
- **Dividends** – is it clear how dividend policies operate in practice and how those policies may be impacted by the risks and capital management decisions facing the company?
- **Low interest rates and fluctuating exchange rates** – have these been taken into consideration in relation to amounts currently reported in the financial statements?
- **Alternative performance measures** – are these well-defined and explained and are statutory measures given appropriate prominence?

**Total of ratings**

**Comments:**



# I. Risk management

Risk management and internal controls are generally considered together by the FRC in the drafting of the Code and supporting Guidance. However, given the increasing importance of each of these areas with the likelihood of a future internal control attestation by management, this seems to be the right time to give each of these critical areas their own section of this framework.

Oversight of risk management is often delegated to the audit committee by the board.

A large part of the considerations regarding risk management should be the increasing impact of technology – critical systems, organisational capabilities, policies, procedures, as well as innovations such as automation and AI. Audit committees will wish to have regular updates on the systems and controls, and keep a watchful reputational eye over the ethical conduct aspects of automation.

Operational resilience, the ability of firms to deal with and learn from operational disruption, is likely to become a topic of increased focus for corporates as it is already for financial services.

Formal requirements in this area are driven by the Code, the Guidance and the Risk Guidance.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

Code provision	Rating 1,2 or 3
11 The audit committee reviews the company's risk management systems (25). This is a requirement unless risk management is expressly addressed by a separate board risk committee composed of independent directors or by the board itself.	
Guidance on audit committees	Rating 1,2 or 3
12 Except where the board or a risk committee is expressly responsible for reviewing the effectiveness of the risk management systems, the audit committee receives reports from management on the effectiveness of the systems they have established and the conclusions of any testing carried out by internal or external auditors (41).	
13 The audit committee considers the level of assurance received on the company's risk management systems and whether this is enough to help the board in satisfying itself that they are operating effectively (42).	
14 The audit committee reviews and recommends to the board the statements included in the annual report in relation to risk management (44).	
Qualitative considerations	Rating 1,2 or 3
15 The audit committee receives a financial risk assessment from management and as a result has a good understanding of how the company identifies, assesses, manages and monitors risk, including how the company sets risk appetite.	
16 The nature, source, format and frequency of information on risk management submitted to the committee and the board is fit for purpose and covers areas that require regular consideration such as tax and treasury.	
17 The audit committee has reviewed the procedures management is using to monitor emerging risks and is satisfied that the company's list of principal risks is being periodically reassessed.	
18 The audit committee is satisfied that an appropriate risk culture has been instilled throughout the company and has considered the impact of reward systems on that risk culture.	
19 The frequency and scope of the audit committee discussions on capital and risk is sufficient and appropriate, taking into account risk arising from strategic and capital management decision-making.	



# I. Risk management

■ Requirements 
 ■ Guidance 
 ■ Qualitative considerations

**1** Area for focus    **2** Performing as expected    **3** Special strength

I10	In fulfilling its oversight role, the audit committee considers whether there are significant events coming up for the company that may introduce new risks and require the introduction of new controls. This could include planned acquisitions, new businesses being launched, outsourcing contracts, or planned divestments.
I11	The audit committee requests 'deep dives' on particular risk hot topics such as cyber, GDPR and climate change bringing in external perspectives to supplement their knowledge and the information provided by management.
I12	The audit committee has a good understanding of the requirements for the firm's ongoing operational resilience, in proportion to the nature of the business. This includes, but is not necessarily limited to, areas such as business continuity, cybersecurity, information technology, internal operations, operational continuity, resilience and strategy, outsourcing, procurement and vendor management, and management of services shared with other group members.
I13	The audit committee ensures there is broad consideration of, and agreement on, the important aspects of operational resilience. This includes those aspects relating to the identification of important business services, mapping and setting impact tolerances, as well as the business's ability to remain within these tolerances.
I14	The nature, source, format and frequency of management information to inform decision-making on operational resilience submitted to the committee and the board is fit for purpose.

**Total of ratings**

**Comments:**



# J. Internal controls

Oversight of internal control is often delegated to the audit committee by the board and the audit committee has responsibility to review the internal financial controls at a minimum.

The increasing importance of technology means that audit committees will wish to have regular updates on the systems and controls, and keep a watchful reputational eye over the ethical conduct aspects of automation.

Following the Kingman report and the Brydon report, a government consultation is expected in due course on an internal controls attestation by management which will increase public focus on this important area. Deloitte's publication [Developing your company's Audit and Assurance Policy](#) includes a framework for developing and reviewing internal controls over financial reporting.

Formal requirements in this area are driven by the Code, the Guidance and the Risk Guidance.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

Code provision	Rating 1,2 or 3
J1 The audit committee reviews the company's internal financial controls and, unless expressly addressed by a separate board risk committee composed of independent directors or by the board itself, the company's internal control systems (25).	
Guidance on audit committees	Rating 1,2 or 3
J2 Except where the board or a risk committee is expressly responsible for reviewing the effectiveness of the internal control systems, the audit committee receives reports from management on the effectiveness of the systems they have established and the conclusions of any testing carried out by internal or external auditors (41).	
J3 The audit committee considers the level of assurance received on the company's internal control systems, including internal financial controls, and whether this is enough to help the board in satisfying itself that they are operating effectively (42).	
J4 The audit committee reviews and recommends to the board the statements included in the annual report in relation to internal control (44).	
Guidance on risk management, internal control and related financial and business reporting	Rating 1,2 or 3
J5 The audit committee ensures that there is broad consideration of, and agreement on, what constitutes a material control including strategic, financial, operational and compliance controls.	
J6 Where a significant failing or weakness has been identified, the audit committee has reviewed and challenged the disclosures on the failing or weakness in the annual report and accounts to ensure that the disclosures are fair, balanced and understandable.	
Qualitative considerations	Rating 1,2 or 3
General controls	
J7 The audit committee has a good understanding of how the company develops, operates and monitors the system of internal control. This includes oversight of risk assessments to understand material financial risks, fraud risks and IT risks, how they are managed and mitigated through strategic, operational, and compliance controls.	
J8 The audit committee considers the maturity of controls around systems used to capture data used for non-financial reporting metrics and key performance indicators in order to establish the reliability of all data used in the annual report.	



# J. Internal controls

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations

**1** Area for focus  
 **2** Performing as expected  
 **3** Special strength

J9	The audit committee is satisfied that there is a clearly defined annual review process of the effectiveness of the system of internal control.
J10	The audit committee has a clear and agreed definition of a significant failing or weakness in internal control which has been shared with management and with internal audit.
J11	Where any significant failings or weaknesses in internal control have arisen, the audit committee has reviewed management's analysis of the root cause and management's action plan to promptly remedy those failings or weaknesses as required by the FRC's Risk Guidance.
J12	The audit committee is planning for the introduction of a requirement in the UK for an attestation regarding internal controls over financial reporting and assessing when a readiness assessment will be needed.
<b>IT controls</b>	
J13	The audit committee receives regular briefings regarding the company's technology strategy and plans, in order to gain an understanding of key systems, data privacy activities, risks and controls, including those associated with cyber security and data management.
J14	The company CISO is invited to attend the audit committee regularly.

**Total of ratings**

**Comments:**



# K. Culture, values, whistleblowing, fraud and investigations

The board has primary responsibility to set the culture, values and ethics of the company. The audit committee should demonstrate commitment to reinforcing a culture of honesty and ethical behaviour through its oversight activities. Its oversight activities should reinforce and provide insight into whether areas within its oversight remit are in line with values and ethics of the company, such as the tone from the top, risk management, entity level controls and oversight of internal controls as a whole. The audit committee's inquiries can therefore help the board judge whether measures put in place to reinforce the desired culture through behaviour are working. Whilst the 2018 Code includes whistleblowing as a board responsibility, the board often delegates oversight of the whistleblowing procedures to the audit committee as this can be time consuming and investigations may be best addressed in committee. Oversight of fraud risk and controls by the audit committee includes considering the potential for override of controls or other inappropriate influence over the financial reporting process by the executive, such as earnings management in order to influence the perceptions of analysts as to the entity's performance and profitability.

Formal requirements in this area are driven by the FRC's Risk Guidance and other FRC materials.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

<b>Other regulatory considerations</b>	<b>Rating 1,2 or 3</b>
K1 The audit committee exercises oversight over management's processes for identifying and responding to the risks of fraud in the entity and has reviewed the key internal controls in place to mitigate the risks of fraud (ISA (UK) 240 (Revised 2021) para 20).	
K2 The audit committee in discussion with the auditor determines whether its responses corroborate or contradict those of management with regard to actual, suspected or alleged fraud (as required by ISA (UK) 240 (Revised 2021) para 21).	
K3 Where necessary, the audit committee's discussions with the auditor should supplement the information provided by management regarding the risks of material misstatement in the financial statements due to fraud, so that a representation may be provided on the following matters (ISA (UK) 240 (Revised 2021) para 39): <ul style="list-style-type: none"> <li>• they have disclosed to the auditor the results of management's assessment of the risk that the financial statements may be materially misstated as a result of fraud;</li> <li>• they have disclosed to the auditor their knowledge of fraud or suspected fraud affecting the entity involving:                             <ol style="list-style-type: none"> <li>i. management;</li> <li>ii. employees who have significant roles in internal control; or</li> <li>iii. others where the fraud could have a material effect on the financial statements; and</li> </ol> </li> <li>• they have disclosed to the auditor their knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.</li> </ul>	
K4 Through its oversight activities, the audit committee is satisfied that the board as a whole can make a representation acknowledging responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and that they believe they have appropriately fulfilled those responsibilities (ISA (UK) 240 (Revised 2021) para 39).	
<b>Guidance on risk management, internal control and related financial and business reporting</b>	<b>Rating 1,2 or 3</b>
K5 The audit committee has assessed on behalf of the board, in considering communication systems relevant to risk management and internal controls, the company's whistle-blowing procedures. <sup>2</sup>	

<sup>2</sup> Under the 2018 Code provision 6, the board should routinely review the means for whistleblowing and the reports arising from its operation. FRC Guidance is expected to reflect this board focus when next updated.





# K. Culture, values, whistleblowing, fraud and investigations

■ Requirements ■ Guidance ■ Qualitative considerations

1 Area for focus 2 Performing as expected 3 Special strength

Qualitative considerations		Rating 1,2 or 3
K6	The audit committee has reviewed the company's Staff Handbook, Code of Conduct or equivalent and is satisfied that it sets an appropriate tone on ethics, and reflects the company values established by the board. If the audit committee becomes aware of behaviours that are not in line with these company values, it takes steps to satisfy itself that these are addressed appropriately and communicated in the annual report.	
K7	The audit committee is satisfied that the company has robust processes for ensuring compliance with regulations within the company's industry sector. Significant regulatory matters are discussed at the board.	
K8	The audit committee receives regular reports on whistleblowing, ethical breaches and non-compliance with laws and regulations, and is satisfied that compliance failures are being dealt with appropriately.	
K9	The audit committee ensures that a fraud risk assessment has been documented by the company and has been provided to the auditors and is satisfied that there are processes in place to ensure that the risks identified are being adequately managed or mitigated.	
K10	The audit committee has discussed their oversight of management's processes for identifying and responding to risks of fraud.	
K11	The audit committee has ensured that the company has appropriate processes and controls in place in response to the UK Bribery Act 2010.	
K12	The audit committee has ensured that the company has reasonable preventative procedures in place in response to the corporate criminal offences relating to tax evasion introduced in the Criminal Finances Act 2017.	
K13	The audit committee receives sufficiently robust management information and metrics to be confident that the information the company publishes relating to transparency in supply chains and the risk of modern slavery is subject to an appropriate level of due diligence.	

**Total of ratings**

**Comments:**



# L. Oversight of internal audit

The audit committee has oversight of internal audit (whether sourced internally or externally) and approves its resources, receives internal audit plans and reports, tracks actions arising and their closure, assesses internal audit effectiveness, and, where there is no internal audit function, considers whether one is required.

The existence of an internal audit function sends a signal about whether an organisation demonstrates a commitment to good control and governance. The audit committee should promote acceptance and understanding of the value of internal audit, by setting a “tone from the top” that the assurance provided by internal audit is desirable, valuable and important.

Expectations of business, technology and the business environment are all changing quickly, which means that new risks are also coming to the fore more quickly. A key role of the audit committee is to continue to challenge the remit and resources of internal audit, to ensure the function is sufficiently dynamic and that specialist skills are available in-house or from an external provider.

In January 2020, the Chartered Institute of Internal Auditors (the IIA) published an Internal Audit Code of Practice covering private and third sector companies. This should be considered by all audit committees and discussed with internal auditors. A section below covers the specific requirements for the audit committee where the IIA Code of Practice has been adopted.

The IIA Code of Practice, implemented appropriately, represents what we consider to be good practice and as a result we present it in place of other qualitative considerations.

Formal requirements in this area are driven by the Code, the Guidance and (where adopted) the IIA Code of Practice. We have retained their different terminology, so chief internal auditor and head of internal audit should be considered interchangeable terms.

■ Requirements ■ Guidance ■ Qualitative considerations

**1** Area for focus **2** Performing as expected **3** Special strength

Code provision	Rating 1,2 or 3
L1 The audit committee monitors and reviews the effectiveness of the internal audit function. If there is no internal audit function, the audit committee considers annually whether there is a need for an internal audit function and makes a recommendation to the board (25).	
L2 If there is no internal audit function, the audit committee can explain how internal assurance is achieved and how this effects the work of external audit (25).	
Guidance on risk management, internal control and related financial & business reporting	Rating 1,2 or 3
L3 In the absence of an internal function, the audit committee assesses whether the other monitoring processes applied by management provide sufficient and objective assurance (47).	
L4 The audit committee reviews and annually approves the internal audit charter to ensure that it is appropriate for the current needs of the organisation (48).	
L5 The audit committee reviews and approves internal audit’s role and mandate, approves the annual internal audit plan and monitors and reviews the effectiveness of its work (48).	
L6 The audit committee ensures that the internal audit plan is aligned to the key risks of the business (49).	
L7 The audit committee pays particular attention to the areas in which work of the risk, compliance, finance, internal audit and external audit functions may be aligned or overlapping and oversee these relationships to ensure they are co-ordinated and operate effectively to avoid duplication (49).	
L8 The audit committee ensures that there is open communication between the different functions and that the internal audit function evaluates the effectiveness of the risk, compliance and finance functions as part of its internal audit plan (50).	
L9 The audit committee ensures that there is open communication between the different functions and that the internal audit function evaluates the effectiveness of the risk, compliance and finance functions as part of its internal audit plan (50).	



# L. Oversight of internal audit

■ Requirements ■ Guidance ■ Qualitative considerations

1 Area for focus 2 Performing as expected 3 Special strength

L10	The audit committee approves the appointment or termination of appointment of the head of internal audit (52).	
L11	Internal audit has access to the audit committee and board chair where necessary and has a reporting line which enables it to be independent of the executive and so able to exercise independent judgement (52).	
L12	The audit committee is satisfied that the quality, experience and expertise of the internal audit function is appropriate for the business (53).	
L13	The audit committee considers the actions management has taken to implement the recommendations of internal audit and whether these properly support the effective working of the internal audit function (53).	
L14	In assessing the work of the internal audit function the audit committee: <ul style="list-style-type: none"> <li>• meets the head of internal audit without the presence of management;</li> <li>• reviews and assesses the annual internal audit work plan;</li> <li>• receives reports on the results of the internal auditor's work; and</li> <li>• monitors and assesses the role and effectiveness of the internal audit function in the overall context of the company's risk management system (54).</li> </ul>	
L15	The audit committee considers whether an independent third party review of internal audit effectiveness and process is appropriate (55).	
<b>IIA Code (if adopted by the company)</b>		<b>Rating</b>
<b>Qualitative considerations (if the IIA Code is not adopted by the company)</b>		<b>1, 2 or 3</b>
L16	The role of internal audit should be articulated in an internal audit charter, which should be publicly available (A6).	
L17	The board, its committees and executive management should set the right 'tone at the top' to ensure support for, and acceptance of, internal audit at all levels of the organisation (A7).	
L18	The scope of internal audit should include information presented to the board and its committees. It should assess whether the information presented to the board and executive management fairly represents the benefits, risks and assumptions associated with the viability of the strategy and corresponding business model (B8, B11).	
L19	The scope of internal audit should include information presented to the board and its committees. It should assess whether the information presented to the board and executive management fairly represents the benefits, risks and assumptions associated with the viability of the strategy and corresponding business model (B8, B11).	
L20	The audit committee should be presented annually with the conclusions of internal audit as to whether the company's risk appetite is being adhered to (B11).	
L21	The audit committee should invite internal audit to meetings to be present and to issue reports as necessary; it should support the right of internal audit to be present at and to present reports at meetings of any other board committees as appropriate (C12).	
L22	In cases where the chief internal auditor has been assigned some other "control" functions the audit committee should ensure that the additional responsibilities of the chief internal auditor: <ul style="list-style-type: none"> <li>• Do not undermine their ability to give appropriate attention to their internal audit responsibilities.</li> <li>• Do not impair their independence from management.</li> <li>• Are appropriately documented in the internal audit charter (D17).</li> <li>• Where the chief internal auditor has responsibilities for other functions in the company, the audit committee should consider whether it is desirable to commission an independent assessment of those functions (D18).</li> </ul>	



# L. Oversight of internal audit

■ Requirements 
 ■ Guidance 
 ■ Qualitative considerations

1 Area for focus 
 2 Performing as expected 
 3 Special strength

L23	<p>The audit committee should take on the following responsibilities and functions:</p> <ol style="list-style-type: none"> <li>a. The primary reporting line for the chief internal auditor should be to the chair of the audit committee who should set the objectives for the chief internal auditor and appraise their performance at least annually (E22, E24).</li> <li>b. The audit committee should be responsible for appointing and removing the chief internal auditor (E23).</li> <li>c. Where the chief internal auditor has been in post for seven years, thereafter annually the audit committee should discuss the chair’s assessment of their independence and objectivity (E24).</li> <li>d. Recommending the remuneration of the chief internal auditor to the remuneration committee and ensuring it is structured in such a way that it avoids conflicts of interest (E25).</li> <li>e. Approving the internal audit budget and disclosing in the annual report whether it is satisfied that internal audit has the appropriate resources (F29, F30).</li> <li>f. Where relevant, the audit committee chair should agree any secondary reporting line for internal audit within the organisation, ensuring it is to someone who promotes, supports and protects internal audit’s independence and objectivity (E27).</li> <li>g. The audit committee should identify appropriate criteria for defining the success of internal audit and should evaluate the performance of the internal audit function on a regular basis (G31).</li> </ol>
L24	<p>The audit committee should obtain an independent and objective external quality assessment at appropriate intervals, as a minimum at least every five years. This should explicitly cover the conformity of internal audit with the IIA guidance. The chair of the audit committee should oversee and approve the appointment process for the independent assessor (G35, G36).</p>

**Total of ratings**

**Comments:**



## M. Oversight of the external audit process

The audit committee has primary responsibility, on behalf of the board, for the tendering, appointment, remuneration, terms of engagement, approval of provision of other services and review of independence and effectiveness of the external auditor. Most of these are legal responsibilities through the Disclosure Guidance and Transparency Rules; others are legal responsibilities for audit committees of the FTSE 350 through the CMA Order.

The audit committee should seek to understand from the auditor the issues they consider significant risks to their audit and those likely to be reported as key audit matters in the audit report. The audit committee should understand the response they intend to implement, the scope of work, materiality and involvement in the work of component (subsidiary) auditors. The audit committee should be prepared to challenge the scope and plans of the external auditor.

In order to ensure the whole external audit process is effective, the audit committee should bear in mind management's role in the audit process through the preparedness for external audit, efficiency of managing the timetable and the quality of papers provided to the external auditor. These factors influence the timeliness, depth and quality of the auditor's work. Management can also promptly respond to queries and address the auditor's proposed adjustments and disclosure deficiencies.

Formal requirements in this area are driven by the Code, the DTR, the Guidance, the CMA Order and the FRC's revised Ethical Standard 2019.

■ Requirements ■ Guidance ■ Qualitative considerations 1 Area for focus 2 Performing as expected 3 Special strength

Code provision		Rating 1, 2 or 3
M1	The audit committee conducts the tender process and makes recommendations to the board about the appointment, reappointment and removal of the external auditor, and approving the remuneration and terms of engagement of the external auditor (25).	
M2	The audit committee reviews and monitors the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements (25).	
M3	The audit committee develops and implements policy on the engagement of the external auditor to supply non-audit services, ensuring there is prior approval, considering the impact this may have on independence, taking into account the relevant regulations and ethical guidance in this regard, and reporting to the board on any improvement or action required (25).	
The Statutory Audit services for Large Companies Market Investigation (Mandatory use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 (the CMA Order) (Applicable to FTSE 350 companies)		Rating 1, 2 or 3
M4	Only the audit committee, acting collectively or through the chair: <ul style="list-style-type: none"> <li>• Negotiates and agrees the statutory audit fee.</li> <li>• Negotiates and agrees the scope of the audit.</li> <li>• Initiates and supervises a competitive tender process.</li> <li>• Makes recommendations to the board of directors on the auditor appointment following a competitive tender process.</li> <li>• Influences the appointment of the audit engagement partner.</li> <li>• Pre-approves the provision of non-audit services by the incumbent auditor (Part 5 of the CMA Order).</li> </ul>	
Guidance on audit committees		Rating 1, 2 or 3
M5	The audit committee assesses annually the qualification, expertise and resources and independence of the external auditors and the effectiveness of the audit process (60).	
M6	The audit committee receives a report on the audit firm's own internal quality control procedures and considers the audit firm's annual transparency report (60).	
M7	Where the external auditor has resigned, the audit committee has investigated the issues giving rise to such resignation and considered whether any action is required (61).	



# M. Oversight of the external audit process

■ Requirements 
 ■ Guidance 
 ■ Qualitative considerations

1 Area for focus 
 2 Performing as expected 
 3 Special strength

M8	The audit committee approves the terms of engagement and the remuneration to be paid to the external auditor, satisfying itself that the level of fee payable in respect of audit services is appropriate and that an effective, high quality, audit can be conducted for such a fee (63 & 65).	
M9	The audit committee reviews and agrees the engagement letter issued by the external auditor at the start of each audit, ensuring that it has been updated to reflect changes in circumstances arising since the previous year (64).	
M10	The audit committee reviews the scope of the external audit and if the audit committee is not satisfied as to its adequacy, it arranges for additional work to be undertaken (64).	
M11	The audit committee monitors the external audit firm's compliance with the Ethical Standard, the level of fees that the company pays in proportion to the overall fee income of the firm, relevant part of it, and other related regulatory requirements (67).	
M12	<p>The audit committee reviews with the external auditors, in a timely manner, the findings of their work [ISA260 para 16]. In particular the audit committee:</p> <ul style="list-style-type: none"> <li>• Discusses major issues that arose during the course of the audit and have subsequently been resolved and those issues that have been left unresolved.</li> <li>• Asks the auditor to explain how they addressed the risks to audit quality identified earlier.</li> <li>• Weighs the evidence they have received in relation to each of the areas of significant judgement.</li> <li>• Reviews key accounting and audit judgements.</li> <li>• Asks the auditor for their perception of their interactions with senior management and other members of the finance team.</li> <li>• Reviews levels of errors identified during the audit, obtaining explanations from management and where necessary the external auditors, as to why certain errors might remain unadjusted (76).</li> </ul>	
M13	The audit committee reviews and monitors management's responsiveness to the external auditor's findings and recommendations (77).	
M14	The audit committee reviews the audit representation letters before signature by management and gives particular consideration to matters where representation has been requested that relate to non-standard issues (77).	
M15	At the end of the annual audit cycle, the audit committee assesses the effectiveness of the audit process (78).	
<b>Qualitative considerations</b>		<b>Rating 1,2 or 3</b>
M16	The audit committee has early discussions with the external auditors to identify significant issues at the earliest opportunity and to discuss the appropriate audit response. The audit committee understands where the auditor will seek specialist resource from the firm, or externally, from outside the core audit practice.	
M17	The audit committee is satisfied that the external audit planning process has involved assessment of accounting policies, feedback on prior year disclosure deficiencies or misstatements and relevant accounting/governance developments.	
M18	<p>In respect of materiality, the audit committee is satisfied that it has a good understanding of: How materiality levels are expected to affect the level of audit work performed in general and in significant risk areas.</p> <ul style="list-style-type: none"> <li>• The benchmarks used in determining materiality levels and why these are considered to be appropriate, focusing on how they reflect the needs and expectations of users of the financial statements.</li> <li>• How auditors are ensuring that materiality is being determined appropriately at group and component levels.</li> <li>• The level at which unadjusted errors are being reported to the audit committee.</li> </ul>	
M19	The audit committee has asked the auditors to explain the overall scope of work in respect of the company's subsidiaries and to explain the extent of their involvement in the work of component (subsidiary) auditors and is satisfied that this is appropriate.	
M20	The audit committee ensures that it understands and is satisfied with the quality and extent of the procedures the auditor has implemented to detect fraud.	



# M. Oversight of the external audit process

■ Requirements 
 ■ Guidance 
 ■ Qualitative considerations

**1** Area for focus    **2** Performing as expected    **3** Special strength

M21	The audit committee has established criteria for its review of the independence of external audit, has considered its responsibilities for auditor objective setting and approval of auditor remuneration, and has ensured it has visibility of all formal recommendations and formal advice supplied by the auditor to ensure independence is maintained.
M22	The audit committee has established criteria for its review of the effectiveness of the external audit process, including in the last year of the auditor's tenure, and has considered the role of management and the audit committee in that process.
M23	The audit committee has asked the auditors whether their audit has been reviewed by the firm's internal quality monitoring processes and, if so, what the main lessons learnt were; how the findings compare with inspection findings; and what actions they have taken to address any matters identified for improvement.

**Total of ratings**

**Comments:**



# N. Going concern and longer term viability

Currently, the board reports on its assessment of the going concern status of the business – will it continue to operate for at least a year and identifying any material uncertainties to the conclusion – and the viability of the business – will the business continue to operate over a longer period determined by the board, drawing attention to any qualifications or assumptions. The audit committee is often asked by the board to provide oversight and advice on these two areas.

The Brydon Report proposes that a Resilience Statement replaces these to provide information about the resilience of the business, including “the likely survival of the company into an indeterminate future.” The audit committee can consider whether it wishes to encourage company reporting to move in this direction.

The proposed structure of the Resilience Statement is that it should cover three time periods:

- A short-term statement over a period of about a year with a high degree of certainty, subject to audit (the equivalent of the current going concern period). This should include the disclosure of material uncertainties that could impact on the company as a going concern before any mitigating action has been taken into account.
- A medium-term statement over a longer period detailing stress-testing or scenario-testing and explaining the directors’ conclusions on that, not subject to audit but with the possibility of the directors obtaining other assurance (similar to disclosure in a proportion of current viability statements).
- A long-term statement about business resilience describing long-term risks and the directors’ analysis of the resilience of the business to those risks, not subject to audit. (This draws together the resilience implications from the current description set out in the strategic report describing how the business will create value over the long term, together with the significant risks).

Formal requirements in this area fall largely on the board, advised by the audit committee. They are driven by the Listing Rules, the Code, the Guidance and the Risk Guidance.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

Code provision	Rating 1,2 or 3
N1      The audit committee reviews and recommends to the board the statements included in the annual report in relation to the viability statement (44).	
Guidance on Risk Management, Internal Control and Related Financial and Business Reporting	
N2      In performing the going concern assessment, the directors consider all available information about the future, the possible outcomes of events and changes in conditions and the realistically possible responses to such events and conditions that would be available to the directors (Appendix A, para 4).	Rating 1,2 or 3
N3      As part of their assessment, the directors determine if there are any material uncertainties relating to events or conditions that might cast significant doubt upon the continuing use of the going concern basis of accounting in future periods (Appendix A, para 5).	
N4      Uncertainties are considered both individually and in combination with others (Appendix A, para 5).	
N5      In determining whether there are material uncertainties, the directors consider: <ul style="list-style-type: none"> <li>• The magnitude of the potential impacts of the uncertain future events or changes in conditions of the company and the likelihood of their occurrence.</li> <li>• The realistic availability and likely effectiveness of actions that the directors would consider undertaking to avoid, or reduce, the impact or likelihood of occurrence of the uncertain future events or changes in conditions.</li> <li>• Whether the uncertain future events or changes in conditions are unusual, rather than occurring with sufficient regularity to make predictions about them with a high degree of confidence (Appendix A, para 6).</li> </ul>	





# N. Going concern and longer term viability

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

N6	For the half-yearly financial statements, directors build on their understanding of these matters since the completion of the last annual report, update their conclusions on the basis of accounting and the existence of material uncertainties and revise their disclosures as necessary (Appendix A, para 10).	
N7	For the longer term viability statement, except in rare circumstances the period chosen is significantly longer than 12 months from the approval of the financial statements. The length of period is determined, taking account of a number of factors, including the board's stewardship responsibilities; previous statements they have made, especially in raising capital; the nature of the business and its stage of development; and its investment and planning periods (Appendix B, para 3).	
N8	The longer term viability assessment includes sufficient qualitative and quantitative analysis, and is as thorough as is judged necessary to make a soundly based statement. Stress and sensitivity analysis has been used to assist the directors in making their statement (Appendix B, para 4).	
N9	The directors consider the individual circumstances of the company in tailoring appropriate analysis best suited to its position and performance, business model, strategy and principal risks. These are undertaken with an appropriate level of prudence, i.e. weighting downside risks more heavily than upside opportunities. This includes analysis of reverse stress, starting from a presumption of failure and seeking to identify the circumstances in which this occurs (Appendix B, para 5).	
N10	Any qualifications or assumptions to which the directors consider it necessary to draw attention in their statement are specific to the company's circumstances, rather than so generic that they could apply to any predictions about the future. They only include matters that are significant to the company's prospects and do not include matters that are highly unlikely either to arise or to have a significant impact on the company. Where relevant, disclosures cross-refer to, rather than repeat, disclosures given elsewhere (Appendix B, para 8).	
N11	The audit committee is satisfied that reporting on going concern and the longer term viability statement gives a fair, balanced and understandable overview of the company's position and prospects (Appendix C).	
N12	The audit committee has reviewed and approved management's assessment of going concern that will be provided to the auditor (ISA (UK) 570).	
<b>Qualitative considerations</b>		<b>Rating 1,2 or 3</b>
N13	The audit committee considers the disclosures in the annual report on principal risks, going concern, viability, the description of the current business model, how the business will create value over the long term, and how opportunities and risks to the future success of the business have been considered and addressed. The audit committee considers there is sufficient, clear information to meet the needs of stakeholders.	
N14	The audit committee is satisfied that the scenarios considered in assessing the longer term viability statement are sufficiently complete and robust and contemplate principal and emerging risks appropriately.	
N15	The audit committee considers that reporting on going concern and the longer term viability statement includes all necessary assumptions and information about scenarios to enable shareholders to understand the quality and completeness of the board's process.	
N16	The audit committee has assessed the gap between the current disclosures on going concern and viability and the disclosures on resilience proposed by the Brydon Report and considers that all materially relevant decision-useful information has been disclosed.	

**Total of ratings**

**Comments:**



# External communication



# O. The audit committee’s communication with shareholders

There should be an annual report on the activities of the audit committee, signed by the audit committee chair, and usually including as a stand-alone report within the corporate governance section of the annual report.

The FRC’s Audit and Assurance Lab project “Audit committee reporting” calls for concise, tailored audit committee reports, telling the story of the audit committee during the year, focusing on the quality and rigour applied by the committee, demonstrated by the actions the audit committee has taken in the furtherance of its role, any changes brought about as a result (i.e. the impact of the committee). Some leading audit committees add the forward looking agenda, the work in progress and the engagement of the audit committee with investors and other stakeholders.

Formal requirements in this area are driven by the Code, the Guidance, the Risk Guidance and the CMA Order.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

Code provision	Rating 1,2 or 3
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The audit committee section of the annual report includes:

- The significant issues that the committee considered in relation to the financial statements and how these issues were addressed.
- An explanation of how it has assessed the independence and effectiveness of the external audit process and the approach taken to the appointment or reappointment of the external auditor, and information on the length of tenure of the current audit firm, when a tender was last conducted and advance notice of any tendering plans.
- O1 • In the case of a board not accepting the audit committee’s recommendation on the external auditor appointment, reappointment or removal, a statement from the audit committee explaining its recommendation and the reasons why the board has taken a different position (this should also be supplied in any papers recommending appointment or reappointment).
- Where there is no internal audit function, an explanation for the absence, how internal assurance is achieved, and how this affects the work of external audit.
- An explanation of how auditor objectivity and independence is are safeguarded if the external auditor provides non-audit services (26).

<b>The Statutory Audit services for Large Companies Market Investigation (Mandatory use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 (the CMA Order) (Applicable to FTSE 350 companies)</b>	Rating 1,2 or 3
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- O2 The audit committee of a FTSE 350 company includes a statement of compliance with the provisions of the CMA Order in each annual audit committee report, with additional disclosures to explain when a tender is expected to take place and why this is in the interests of the company’s members where there has not been a competitive tender for five consecutive financial years (The CMA Order 7.1, 4.1-4.4).



# O. The audit committee’s communication with shareholders

■ Requirements 
 ■ Guidance 
 ■ Qualitative considerations

1 Area for focus 
 2 Performing as expected 
 3 Special strength

<b>Guidance on Audit Committees</b>	<b>Rating 1,2 or 3</b>
<p>In addition to the content required by the Code, the audit committee section of the annual report also includes:</p> <ul style="list-style-type: none"> <li>• A summary of the role of the audit committee.</li> <li>• How the audit committee composition requirements have been addressed, and the names and qualifications of all members of the audit committee during the period.</li> <li>• The number of audit committee meetings.</li> <li>• How the audit committee's performance evaluation has been conducted.</li> <li>• Advance notice of any retendering plans.</li> <li>• The nature and extent of any interaction with the FRC's Corporate Reporting Review team.</li> </ul>	
<p>O3 • Where a company's audit has been reviewed by the FRC's Audit Quality Review team and significant findings have been raised, the committee should make disclosures about the findings and the actions they and the auditors plan to take. The discussion should not include disclosure of the audit quality category.</p> <ul style="list-style-type: none"> <li>• An explanation of how the committee has assessed the effectiveness of internal audit and satisfied itself that the quality, experience and expertise of the function is appropriate for the business.</li> <li>• The committee's policy for approval of non-audit services.</li> <li>• The audit fees for the statutory audit of the company's consolidated financial statements paid to the auditor and its network firms for audit related services and other non-audit services, including the ratio of audit to non-audit work.</li> <li>• For each significant engagement, or category of engagements, an explanation of what the services are and why the audit committee concluded that it was in the interests of the company to purchase those services from the external auditor (81).</li> </ul>	
<p>O4 The audit committee report is signed by the audit committee chair (80).</p>	
<p>O5 The audit committee report does not repeat information disclosed elsewhere in the annual report, it provides signposts to that information (84).</p>	
<p>O6 The chair of the audit committee is present at the AGM to answer questions on the separate section of the annual report describing the audit committee's activities and matters within the scope of the audit committee's responsibilities (85).</p>	
<b>Guidance on Risk Management, Internal Control and Related Financial and Business Reporting</b>	<b>Rating 1,2 or 3</b>
<p>O7 The audit committee ensures that where any significant failings or weaknesses in internal control or risk management have arisen, there is a suitable explanation of what actions have been or are being taken to remedy any significant failings or weaknesses (Guidance on Risk Management, 58).</p>	



# O. The audit committee's communication with shareholders

■ Requirements ■ Guidance ■ Qualitative considerations

1 Area for focus 2 Performing as expected 3 Special strength

Qualitative considerations		Rating 1,2 or 3
O8	The audit committee acknowledges and embraces its role of protecting the interests of shareholders as regards the integrity of published financial information by the company and the effectiveness of audit.	
O9	The audit committee chair demonstrates personal ownership and accountability for the audit committee report by personally authoring or editing the report, and ensuring that the work of the audit committee during the year is reflected.	
O10	The audit committee report details the committee's review of significant risks or key judgement areas, including sources of evidence and assurance, allowing readers insight into how issues have been addressed and the rationale behind the audit committee's conclusions, rather than simply stating they were considered.	
O11	The audit committee considers whether there is additional "decision-useful information" – data useful for facilitating prediction – that should be provided in its report to supplement the information in the remainder of the annual report.	
O12	The audit committee reviews all internal audit "red reports" to determine if they arise from significant failings or weaknesses in internal control requiring disclosure in the annual report and accounts.	
O13	The audit committee report details specific activities undertaken by the committee during the course of the year, including material areas where the audit committee has found it necessary to raise challenges to executive management, in order to enhance communication with shareholders about the work of the committee.	
O14	The audit committee report includes updates on work in progress items, particularly where action is being taken to remediate areas of risk management and internal controls.	
O15	The audit committee reports on the future agenda, in particular explaining which areas it intends to focus on in the coming year, or on a rotational basis.	
O16	The audit committee chair offers to meet significant investor bodies to discuss committee matters.	
O17	If the board holds a stakeholder session, the audit committee chair offers to attend to take questions from other stakeholders on committee matters.	
O18	The audit committee or the audit committee chair actively and regularly engages with the workforce engagement mechanism established by the Code to determine whether there is any input that should change the role, remit, audit and assurance policy or other planned activities of the audit committee.	

**Total of ratings**

**Comments:**



# Deep dives



# P. Deep dive – the public interest: consideration of wider stakeholders

Companies Act 2006 s172 sets out the duty of each director to promote the success of the company for the benefit of the shareholders as a whole. The broader matters required to be considered by directors when they steer the company for success on behalf of its owners include due consideration in decision making of longer term consequences, stakeholders, community, environment and business conduct.

The s172(1) statement in the annual report is an opportunity for directors to demonstrate how they are leading a responsible, long term business.

The importance of considering a broad range of stakeholders is reflected also in the Brydon review. Aiming to “improve trust in its entirety”, the report recommends that the directors present an annual ‘Public Interest Statement’ in the strategic report - essentially a narrative which provides “an opportunity for directors to articulate in a holistic way how the company they govern serves the wider public interest” and how the company has managed this in the year under review. The inclusion of such a statement does not require a change in the law and a board may of course choose to provide it voluntarily, perhaps as a lead in to the s172(1) statement.

Formal requirements in this area relate to reporting rather than to the specific role of the audit committee. They are driven by the Companies Act 2006 and by the FRC’s Guidance on the Strategic Report.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

	Qualitative considerations	Rating 1, 2 or 3
P1	The audit committee has considered the disclosures in the front half of the annual report regarding corporate purpose. The audit committee considers this has been clearly articulated alongside the company’s strategy and values, and that the annual report explains how purpose, strategy and values are aligned with the company’s culture.	
P2	The audit committee is satisfied that there is adequate explanation of how the board has considered the interests of a broader group of stakeholders, as set out in s172 of the Companies Act 2006, in fulfilling its duties.	
P3	<p>The audit committee is satisfied that there is adequate explanation of how the board has considered the interests of a broader group of stakeholders, as set out in s172 of the Companies Act 2006, in fulfilling its duties.</p> <p>In considering this, the audit committee reviews whether the statement includes in relation to each significant decision taken by the board:</p> <ul style="list-style-type: none"> <li>• The likely consequences of any decision in the long term.</li> <li>• The interests of the company’s employees.</li> <li>• The need to foster the company’s business relationships with suppliers, customers and others.</li> <li>• The impact of the company’s operations on the community and the environment.</li> <li>• The desirability of the company maintaining a reputation for high standards of business conduct.</li> <li>• The need to act fairly as between members of the company.</li> </ul>	



# P. Deep dive – the public interest: consideration of wider stakeholders

■ Requirements ■ Guidance ■ Qualitative considerations      1 Area for focus   2 Performing as expected   3 Special strength

P4	The audit committee is satisfied with the quality of the management information underlying the s172(1) statement and any KPIs or metrics provided. The audit committee has considered whether to request any internal or external assurance in this area.
P5	Where the board has chosen to provide a Public Interest Statement, the audit committee is satisfied that the statement is an appropriate description of how the company serves the public interest and how it has managed that in the year under review. The audit committee has considered whether to request any internal or external assurance in this area.

**Total of ratings**

**Comments:**





## Q. Deep dive – climate change

Investors, regulators and government are increasingly focused on the health of our planet. In the UK, for December 2021 year ends onwards almost all listed companies will likely be required to report using the TCFD framework.

The FRC has already highlighted its expectation that boards will report on how they have taken into account the resilience of the company's business model and risks, uncertainties and viability in the light of climate change, including the impact on asset valuation and impairment testing assumptions.

Major investors have issued position papers, public letters and communications targeted at boards, CEOs, AC Chairs and auditors regarding climate change.

This series of supplementary questions to assess audit committee effectiveness allows audit committees to consider how far their approach represents leading practice.

Code provision <sup>3</sup>	Rating 1,2 or 3
Q1 The board should assess the basis on which the company generates and preserves value over the long-term. It should describe in the annual report how opportunities and risks to the future success of the business have been considered and addressed, the sustainability of the company's business model and how its governance contributes to the delivery of its strategy (1).	
Q2 The board should carry out a robust assessment of the company's emerging and principal risks. The board should confirm in the annual report that it has completed this assessment, including a description of its principal risks, what procedures are in place to identify emerging risks, and an explanation of how these are being managed or mitigated (28).	
FRC's Summary of key developments for 2020/21 annual reports	Rating 1,2 or 3
Q3 The strategic report clearly describes environmental policies, rather than simply naming or listing them.	
Q4 Clear explanations are included for terminology such as 'net zero' or 'Paris compliant' and it is clear which emissions are included in any emissions targets, how progress will be measured and reported, and what assurance will be sought.	
Q5 A balanced description of how climate policies and targets have been incorporated into business plans and their expected business impact, is included in the strategic report, making appropriate use of key performance indicators, where relevant, and without disproportionate focus on 'good news' stories in parts of the business that are not material.	
Q6 A description is included of the impact of the business on the environment, including their supply chains.	
Q7 Companies should provide required segmental and disaggregated revenue disclosures to enable users to understand the relative sizes of operations for which climate change presents substantially different risks and opportunities.	
Q8 The financial statements should, where relevant, explain the impact of climate related risks, policies and strategies on both measurement and disclosure including, in particular: <ul style="list-style-type: none"> <li>• impairment of individual assets as well as cash generating units;</li> <li>• useful economic lives of assets;</li> <li>• expected amounts and timing of cash outflows for provisions and other liabilities;</li> <li>• fair values of assets and liabilities; and</li> <li>• disclosure of key accounting judgements, estimation uncertainties and related sensitivities.</li> </ul>	

<sup>3</sup> At the time of writing there is not yet a requirement to report on climate change specifically, however there are many reporting requirements that may prompt companies to disclose climate-related issues. These Code provisions are part of a portfolio of requirements including strategic report disclosures requiring consideration of environmental matters such as the non-financial information statement and the s172(1) statement.



# Q. Deep dive – climate change

■ Requirements 
 ■ Guidance 
 ■ Qualitative considerations

1 Area for focus 
 2 Performing as expected 
 3 Special strength

FRC's Climate Thematic Review 2020 – Governance		Rating 1,2 or 3
Q9	The audit committee considers whether the annual report has included a clear explanation of the company's governance structure and oversight of climate matters. Note that the more developed reporters link these insights to the TCFD framework.	
Q10	The audit committee considers whether the annual report has included with regard to committee structure: <ul style="list-style-type: none"> <li>the selection process for the climate expert or body;</li> <li>any relevant training members had received; and</li> <li>explanations of the process by which the board received climate-related information.</li> </ul>	
Q11	The audit committee considers whether the annual report has information on board and committee monitoring of climate-related risks and opportunities, including: <ul style="list-style-type: none"> <li>reporting on examples of specific climate-related issues discussed by relevant company bodies, how those issues could impact the business and the reasoning behind any related decisions; and</li> <li>where relevant, reporting on remuneration linked to the achievement of sustainability and climate change targets as key part of governance.</li> </ul>	
Qualitative considerations		Rating 1,2 or 3
Q12	The audit committee considers that its responsibility for the integrity of corporate reporting extends to material climate-related risks, opportunities, governance and strategy and that these have been disclosed and adequately reflected throughout the annual report and financial statements.	
Q13	The audit committee considers that the company's procedures for identifying emerging risks can successfully identify and assess material climate-related risks, covering both physical and transition risks.	
Q14	The audit committee uses a recognised framework such as the COSO ESG framework to assist it in identifying and assessing climate-related risks.	
Q15	The audit committee has assessed management's forecasting and scenario testing on climate-related risks in the light of recognised scenario data (for example, published by the Bank of England). The audit committee considers the scenarios to be robust and that they may therefore be used in key judgements and estimates on valuations and impairments.	

**Total of ratings**

**Comments:**



## R. Deep dive – cyber risk

Cybersecurity is amongst the most complex and rapidly evolving issues companies must continually address. Mobile technologies, cloud computing and social media have led to major breaches of proprietary information and damage to organisational IT infrastructure and have transformed the IT risk landscape at a rapid pace.

The audit committee will often support the board by providing oversight of the effectiveness of the process to identify key risks and to ensure that the associated material controls to manage or mitigate those key risks are sufficiently robust. Few companies do not list cyber risk – including cybercrime, ransomware and data theft or misappropriation – as a critical risk to their business.

There is no specific disclosure guidance in the UK, although both investors and the FRC have mentioned cyber risk as one risk that should be considered when reporting on principal risks and uncertainties. The FRC's Guidance on the Strategic Report uses cyber risk as an example of disclosure on changes in the risk profile of an entity. It explains that risk disclosures should identify where a risk has increased, explain the ways in which the risk could affect the business - "for instance, a cyberattack, loss of sensitive data leading to a lack of customer confidence, a failure of IT systems leading to a failure to operate certain elements of the business..." The mitigation description should explain how mitigation has addressed the increased risk profile.

This series of supplementary questions to assess audit committee effectiveness allows audit committees to consider how far their approach represents leading practice.

■ Requirements ■ Guidance ■ Qualitative considerations

1 Area for focus 2 Performing as expected 3 Special strength

Qualitative considerations		Rating 1,2 or 3
R1	The audit committee recognises that its remit overseeing risk management activities and monitoring management's policies and procedures plays a significant strategic role in assessing the efficacy of cyber risk initiatives and policies.	
R2	The audit committee receives regular briefings regarding the company's technology landscape, including key systems, data privacy activities, risks and controls and the risk associated with cyber security and data management and uses these briefings to assess the effectiveness of risk management and internal controls in this area.	
R3	The audit committee considers that the company's procedures for identifying emerging risks can successfully identify and assess material cyber risks, including cyber-crime and data theft, the nature of the likely perpetrators or facilitators of any attack (including internal personnel).	
R4	The audit committee has a trusted expert internal or external advisor that it can call upon as part of its oversight activities. This expert is sufficiently familiar with the company's strategy to help identify cyber risks and advise on associated controls and its three lines of defence model in this area.	
R5	The audit committee considers that its responsibility for the integrity of corporate reporting extends to material cyber risks, together with associated opportunities, governance and strategy, and that these have been disclosed and adequately reflected in the annual report.	
R6	The audit committee assesses whether it requires more assurance over cyber risks or over annual report disclosures and where necessary has taken steps to involve internal audit or external assurance providers.	

**Total of ratings**

**Comments:**



# S. Deep dive – data privacy

The General Data Protection Regulation (GDPR) was implemented in May 2018 and most boards and audit committees put significant efforts to reach compliance by that date. Many have continued their governance procedures since then, and integrated data privacy compliance into their existing processes.

In the UK, the Information Commissioner’s Office (ICO) governs the data protection rules, assesses breaches and imposes fines. Initial fines announced were very high.

The ICO indicates that it expects companies to have “an organisational structure for managing data protection and information governance, which provides strong leadership, clear reporting lines and responsibilities, and effective information flows. This could mean clear management roles and responsibilities for staff in the information security or records management departments.”

Formal requirements in this area fall largely on the board, often supported by the audit committee. They are driven by the GDPR.

This series of supplementary questions to assess audit committee effectiveness allows audit committees to consider how far their approach represents leading practice.

■ Requirements  
 ■ Guidance  
 ■ Qualitative considerations  
 1 Area for focus  
 2 Performing as expected  
 3 Special strength

Qualitative considerations		Rating 1,2 or 3
S1	The audit committee considers that decision-makers, such as the board or executive committee, demonstrably show overall responsibility for data protection and information governance, they lead by example and promote a proactive, positive culture of data protection compliance.	
S2	The audit committee is satisfied that there are clear reporting lines and information flows between relevant groups; such as from the management board to the audit committee, or from an executive team to an information governance steering group, such that compliance with the GDPR’s governance requirements can be proactively demonstrated should that be necessary.	
S3	The audit committee receives regular briefings regarding the company’s level of technology and digitisation, key systems, data privacy activities, risks and controls and is satisfied that there is a good understanding of where, how, and why the company processes personal data and good evidence of the thoroughness of its current compliance with GDPR.	
S4	The audit committee has satisfied itself that the company’s level of security due diligence is appropriate for acquisitions and for trading partners, including external suppliers.	
S5	The audit committee considers that the company’s procedures for identifying emerging risks can successfully identify and assess new material data privacy risks.	
S6	The audit committee assesses whether additional expertise is required to support internal audit.	
S7	The audit committee assesses whether it requires more assurance over data privacy risks or over annual report disclosures and where necessary has taken steps to involve internal audit or external assurance providers.	

**Total of ratings**

**Comments:**



# Finalising your self-assessment

To help you pull together the results of your assessment and to facilitate comparison with the views of your fellow audit committee members, you can complete this summary of your findings in the different areas. The expected score for each section is the total of scoring "performing as expected" – a 2 – for each item in the framework. The scoring is merely a prompt to revisit a section and to review areas of activity you have flagged for attention.

	Expected score	Your total	Areas to follow up
<b>Setting up for success</b>			
A – Establishment, membership and appointment	18		
B – The audit committee chair	12		
C – Skills, experience, training and mindset	12		
D – Meetings of the committee	20		
E – Support and resources	10		
F – Relationship with the board	18		
G – Establishing an audit and assurance policy	12		
<b>Subtotal – Setting up for success</b>	<b>102</b>		
<b>The audit committee agenda</b>			
H – Oversight of accounting judgements, business and financial reporting and other company announcements	42		
I – Risk management	28		
J – Internal controls	28		
K – Culture, values, whistleblowing, fraud and investigations	26		
L – Oversight of internal audit	48		
M – Oversight of the external audit process	46		
N – Going concern and longer term viability	32		
<b>Subtotal – The audit committee agenda</b>	<b>250</b>		
<b>External communication</b>			
O – The audit committee's communication with shareholders	36		
<b>Subtotal – External communication</b>	<b>36</b>		
<b>Total (excluding deep dives)</b>	<b>388</b>		
<b>Deep dives</b>			
P – The public interest: consideration of wider stakeholders	10		
Q – Climate change	30		
R – Cyber risk	12		
S – Data privacy	14		
<b>Subtotal - Deep dives</b>	<b>66</b>		
<b>Total (including deep dives)</b>	<b>454</b>		

## Focus areas identified



# Glossary – abbreviations

**Brydon report** – [“Assess, assure and inform” Improving audit quality and effectiveness: Report of the independent review into the quality and effectiveness of audit](#) – December 2019

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**Code** – [The 2018 UK Corporate Governance Code](#), published by the FRC

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**CMA Order** – [The Statutory Audit Services for Large Companies Market Investigation \(Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities\) Order 2014](#) (Applicable to FTSE 350 companies)

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**DTR** – [Disclosure Guidance and Transparency Rules](#), published by the FCA

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**ES** – [Revised Ethical Standard 2019](#), published by the FRC

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**Guidance** – [2016 Guidance on Audit Committees](#), published by the FRC

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**IIA Code of Practice** – [Internal Audit Code of Practice: Guidance on effective internal audit in the private and third sectors](#)

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**Kingman report** – [Independent review of the Financial Reporting Council](#) – December 2018

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**Risk Guidance** – [2014 Guidance on Risk Management, Internal Controls and Related Financial and Business Reporting](#), published by the FRC

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**TCFD** – Financial Stability Board’s [Task Force on Climate-related Financial Disclosures](#)



# Contacts

If you would like to contact us please email [corporategovernance@deloitte.co.uk](mailto:corporategovernance@deloitte.co.uk) or use the details provided below:



**Tracy Gordon**

Tel: +44 (0) 20 7007 3812  
Mob: +44 (0) 7930 364431  
Email: [trgordon@deloitte.co.uk](mailto:trgordon@deloitte.co.uk)



**Corinne Sheriff**

Tel: +44 (0) 20 7007 8368  
Mob: +44 (0) 7824 609772  
Email: [csheff@deloitte.co.uk](mailto:csheff@deloitte.co.uk)



**William Touche**

Tel: +44 (0) 20 7007 3352  
Mob: +44 (0) 7711 691591  
Email: [wouche@deloitte.co.uk](mailto:wouche@deloitte.co.uk)

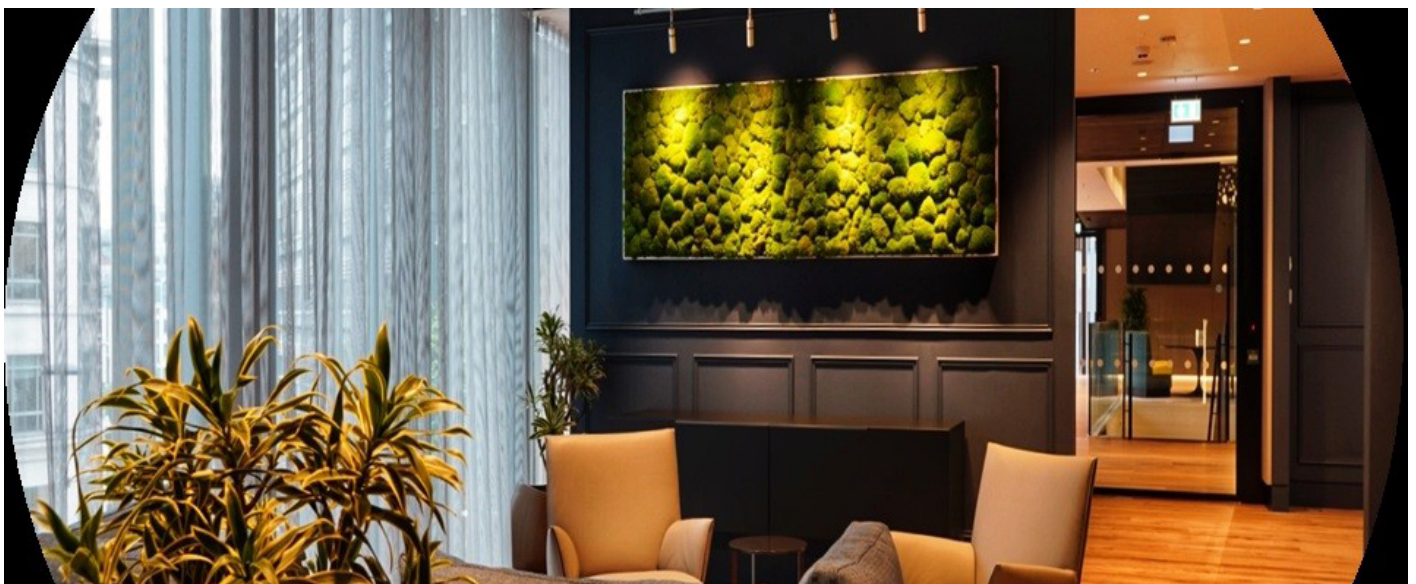


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