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Section 1
Audit committee
leading practices
and trends
The following is a summary of certain leading practices for audit committees. It is not all inclusive, but it can be used to help assess audit committee practices and to discuss agendas and other considerations.

Committee dynamics

• Focus on committee composition, including independence, financial expertise, risk management, broad business or leadership experience, and succession planning.
• Limit the number of audit committee members to four or five to optimise effectiveness.
• Oversee and respond to enterprise risk management activities.
• Conduct an annual committee self-evaluation.
• Consider periodically rotating audit committee members, including the chairman.
• Encourage discussion, rather than presentation, at meetings.
• Participate in audit committee education activities.
• Engage independent advisers when needed.

Risk oversight

• Increase the focus on risk oversight and assessment.
• Avoid becoming overly dependent on forms or tools for monitoring risk.
• Periodically reassess the list of top risks, determining who in management and which board committee is responsible for each.
• Evaluate information technology (IT) projects, including IT milestones and reporting against them, especially for IT transformation.
• Consider post-acquisition reviews, including risks, relevant integration milestones, and return on investment (ROI) analysis to evaluate the reliability of initial acquisition assumptions.
• Have appropriate leaders in the business make a presentation at a board or audit committee meeting to enhance the members’ understanding of the business and risks and to evaluate the depth of talent.
Self-assessment and evaluation of effectiveness

• Perform a self-assessment in a thorough manner rather than as a compliance exercise.
• Consider using self-assessment results as a catalyst to re-engineer processes, procedures, and agendas, which should influence where the audit committee spends its time.
• Communicate with the board on activities and recommendations.
• Align audit committee meeting materials and agendas with priority areas:
  - Put significant areas first in advance materials and on the agenda.
  - Include matters for review and comment.
  - Present compliance matters, standard reports, and informational items at the end of advance materials and meetings; they may not need to be discussed at the meeting.
  - Meetings should be preceded or followed by private and executive sessions, absent members of management.

Oversight of internal controls, financial reporting and integrated reporting

• Understand key controls and reporting risk areas as assessed by financial management, the internal auditors, and the independent auditor.
• Emphasise oversight of corporate taxes, an area where high-risk and big-money decisions are made.
• Leverage the value of internal controls beyond compliance.
• Consider levels of authority and responsibility in key areas, including pricing and contracts, acceptance of risk, commitments, and expenditures.
• Understand complex accounting and reporting areas and how management addresses them.
• Understand significant judgments and estimates used by management and their impact on the financial statements, such as fair-value accounting and related assumptions.
• Anticipate and understand how regulatory developments and reporting developments in the areas of financial, sustainability reporting and integrated reporting may affect the company, particularly its talent needs.
Interaction with the independent auditor

• Exercise ownership of the relationship with the independent auditor.
• Get to know the lead partners and meet periodically with specialists (e.g., tax, IT, actuarial, regulatory).
• Establish expectations regarding the nature and method of communication, as well as the exchange of insights.
• Engage in regular dialogue outside the scheduled meetings.
• Set an annual agenda with the independent auditor.
• Focus on independence, including a preapproval process.
• Provide formal evaluations and regular feedback.

Partnership with the CFO and other management

• Focus on the tone at the top, culture, ethics, and hotline monitoring.
• Conduct annual evaluations.
• Engage in the identification of potential issues.
• Understand plans to address new accounting and regulatory reporting requirements.
• Provide input to management’s goal-setting process.
• Discuss succession planning for the CFO and staff.
• Conduct pipeline and staff reviews, including identification of high potential personnel.

Executive (private) sessions

• Schedule regular sessions with the internal auditors, the independent auditor, and management.
• Provide clear objectives and expectations for each meeting.
• Prepare specific topics and questions.
• Understand the response to and resolution of each issue raised.
Executive compensation

• Periodically conduct meetings with the remuneration committee regarding management incentives.
• Work with the remuneration committee to consider the incentive structure and whether it contributes to increased fraud risk.
• Increase focus on the compensation of officers and directors, including the appropriate use of corporate assets such as planes and apartments.

Interaction with the internal auditors

• Assess whether the internal auditors have a direct reporting line to the audit committee and an indirect line to management for administrative activities.
• Be involved with the internal audit risk assessment and audit plans, including activities and objectives regarding internal control over financial reporting.
• Conduct annual evaluations.
• Understand internal audit staffing and succession planning.

Orientation and continuing education

• Address board education in the company’s corporate governance guidelines to be consistent with JSE listing requirements.
• Provide orientation of new members that involves company executives, internal audit, and the independent auditor.
• Offer on-going one-on-one or committee-level education opportunities.
• Consider offering continuing education in specialised or regulated industry matters, reporting, operations, and related topics.
Audit Committee composition
Audit committees should regularly review their composition and membership to confirm that they encompass the knowledge and experience needed to be effective. In addition to industry knowledge, committee members should have a strong grasp of key financial reporting and accounting issues, such as going concern, revenue recognition, areas of significant judgment including goodwill measurements and accounting for intangible assets, pensions and other post-employment benefits, financial instruments and other critical accounting policies, including how these policies compare to industry practices. Internal controls relevant to financial reporting are particularly important since these form the basis for the prevention and detection of fraud or error in financial reporting.

Appointment of the audit committee

The King Code of Governance Principles and the King Report on Governance (King III) emphasise the vital role of an audit committee in ensuring the integrity of financial controls and integrated reporting, and identifying and managing financial risk. This sentiment is echoed in the Companies Act, 2008 (Act No 71 of 2008) (the Companies Act or the Act). The appointment of an audit committee is regulated as part of the enhanced accountability and transparency requirements set out in Chapter 3 of the Companies Act (Chapter 3).

The Companies Act requires certain categories of companies to appoint an audit committee. Public companies and state owned companies must appoint an audit committee. In addition, any other types of companies (private company, personal liability company or non-profit company) that provide for the appointment of an audit committee in their Memorandum of Incorporation must comply with the relevant provisions of the Act to the extent provided for in the Memorandum of Incorporation. In our experience, very few private companies choose to include a requirement in its Memorandum of Incorporation for the appointment of an audit committee.
Notwithstanding the requirements of the Companies Act, King III proposes that ALL companies should have an audit committee.

The Companies Act states that, where the appointment of an audit committee is required, the audit committee must be appointed by the shareholders at every annual general meeting. This means that the appointment of the audit committee becomes an annual event. This requirement highlights the importance of the board’s nomination committee. As all audit committee members must be directors (members of the board), it is important that the nominations committee identifies suitably skilled and qualified individuals to nominate for appointment to the audit committee. Of course, the shareholders may appoint any director they deem fit and proper.

Section 94 of the Companies Act determines that the audit committee must consist of at least three members who must be directors of the company and not:
• be involved in the day to day management of the company for the past financial year;
• be a full-time employee for the company for the past 3 financial years;
• be a material supplier or customer of the company such that a reasonable and informed third party would conclude in the circumstances that the integrity, impartiality or objectivity of that director is compromised by that relationship; and
• be related to anybody who falls within the above criteria.

The requirements of section 94 are prescriptive. It would appear that should the company appoint an audit committee with persons other than those prescribed, it would not be an audit committee as required by the Companies Act. As a result, any functions undertaken by a non-compliant (that is an “improperly constituted”) audit committee will not have been performed by the audit committee as required by the Companies Act. This may impact the actions of the committee, and may even result in liability for the committee members.

The audit committee can consist of as many members as the company wishes to appoint (but at least three), but each member must meet the criteria and must be a director of the company. The audit committee may utilise advisors and obtain assistance from other persons inside and outside of the company. The audit committee may also invite knowledgeable persons to attend its meetings. However, the formally appointed members of the audit committee entitled to vote and fulfil the functions of the audit committee will have to meet the criteria (non-executive independent directors) in accordance with the prescribed requirements.
Ethical leadership and social responsibility is highlighted in King III. These same sentiments are echoed in the Companies Act. Although it may be argued that the provisions of the Companies Act are onerous and prescriptive, it should be acknowledged that the intention is for the audit committee to play a key role in ensuring accountability and transparency. As an independent, objective body, it should function as the company’s independent watchdog to ensure the integrity of financial controls, combined assurance, effective financial risk management, and meaningful integrated reporting to shareholders and stakeholders alike.

King III proposes that every company appoints an audit committee comprising at least three independent non-executive directors.

The JSE requires listed companies to appoint an audit committee in compliance with King III. With regard to the composition of the audit committee, the committee must comprise at least three independent non-executive directors. If an issuer has an independent non-executive chairman of the board, he/she may be a member of the audit committee, subject to the following provisions:

- all the other members of the audit committee (at least two) are independent non-executive directors
- he/she may not be the chairman of the audit committee
- the dual role (chairman of the board and member of the audit committee) is specifically disclosed to shareholders at the annual general meeting referred to in Section 94(2) of the Act,
- shareholders approve the appointment of the chairman to the audit committee at the annual general meeting.

Independence of audit committee members

The independence of audit committee members should be subject to review at least annually and more often as necessary. Companies that are required, in terms of the Companies Act, to appoint an audit committee should have policies in place to facilitate timely identification of changing relationships or circumstances that may affect the independence of audit committee members. Many companies require directors to complete an independence questionnaire when appointed to the board and annually thereafter, and to notify the company of any changes that may affect independence. For audit committee members, these questionnaires should be tailored to reflect the independence criteria set out in principle 2.18 of King III and the Companies Act, as summarised below.
Companies may want to involve legal counsel in assessing the independence of directors. Regardless, the Companies Act requires the annual appointment of the audit committee, which provides an ideal opportunity for the nominations committee to re-assess the independence of the audit committee members.

The Companies Act and King III require audit committee members to be independent

In this regard, cognisance should be taken of the position of shareholders as potential members of the audit committee. The Companies Act makes no reference to shareholding as a disqualification from membership of the audit committee, and the value judgment pertaining to independence relates only to suppliers and customers. The mere fact that a person holds shares in the company would not, on its own, preclude such a person from serving on the audit committee. However, it is proposed that, in line with the best practice principles set out in King III, the appointment of shareholders to the audit committee should be carefully considered. A judgment on the effect of the shareholding or other relationships is required in order to establish the likely factual impact on the independence of a particular person.

For listed companies, the definition of independence as set out in King III will apply. The JSE makes it clear that some listed companies combine the audit and risk committee. (The risk committee must have a minimum of three members. Membership of the risk committee should include executive and non-executive directors. The chairman of the board may me a member of this committee but must not chair it.) Given the difference in the membership of these committees, companies must ensure that in these instances the membership of the combined committee meets the more stringent independence criteria of the audit committee as set out in King III.
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<th><strong>King III – Independent if:</strong></th>
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<td>The director was not involved in the day-to-day management of the business for the previous financial year.</td>
<td>The director is not a representative of a shareholder who has the ability to control or significantly influence management or the board.</td>
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<tr>
<td>The director was not a full time employee or prescribed officer of the company or a related company during the previous three financial years.</td>
<td>The director does not have a direct or indirect interest in the company (including any parent or subsidiary in a consolidated group with the company) which exceeds 5% of the group’s total number of shares in issue.</td>
</tr>
<tr>
<td>The director is not a material supplier or customer of the company such that a reasonable and informed third party would conclude in the circumstances that the integrity, impartiality or objectivity of that director is compromised by that relationship.</td>
<td>The director does not have a direct or indirect interest in the company which is less than 5% of the group’s total number of shares in issue, but is material to his personal wealth.</td>
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<tr>
<td>The director is not related to anybody who falls within the above criteria.</td>
<td>The director is not a professional adviser to the company or the group, other than as a director.</td>
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<td>The director has not been employed by the company or the group of which it currently forms part in any executive capacity, or appointed as the designated auditor or partner in the group’s external audit firm, or senior legal adviser for the preceding three financial years.</td>
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<tr>
<td></td>
<td>The director is not a member of the immediate family of an individual who is, or has during the preceding three financial years, been employed by the company or the group in an executive capacity.</td>
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<td></td>
<td>The director is free from any business or other relationship (contractual or statutory), which could be seen by an objective outsider to interfere materially with the individual’s capacity to act in an independent manner, such as being a director of a material customer of or supplier to the company.</td>
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<td>The director does not receive remuneration contingent upon the performance of the company.</td>
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Qualifications and financial literacy

King III requires that the audit committee should, as a collective, have the necessary skill and experience to meet its obligations. This should be considered by the nominations committee prior to the AGM when they nominate members for appointment to the audit committee.

As a collective, the audit committee must have a good understanding of:
• integrated reporting, which includes financial reporting
• internal financial controls
• external audit process
• internal audit process
• corporate law
• risk management
• sustainability issues
• information technology governance, and
• the general governance processes within the company.

The Companies Act requires at least one third of the members of the audit committee to have academic qualifications, or experience in economics, law, corporate governance, finance, accounting, commerce, industry, public affairs or human resource management.

Audit committee financial literacy recommendations

• Self-assessment should be thorough, not merely a compliance exercise, and should be repeated periodically
• Members should understand auditing, accounting, and financial reporting issues relevant to the company and how management and the independent auditor address them
• Committees should anticipate and understand how pending financial reporting and regulatory developments may affect the company, and particularly its talent needs
• Members should focus on committee composition, including independence, financial expertise, risk management, broad business or leadership experience, and succession planning
In order for the audit committee to function optimally, it is necessary for the members to be financially literate. In this regard, it is proposed that at least one member of the audit committee have a detailed understanding of financial reporting, which may include:

• an understanding of financial statements and financial reporting standards (IFRS)
• an ability to assess the general application of IFRS in connection with the accounting for estimates, accruals, and reserves
• experience preparing, auditing, analysing, or evaluating financial statements that present a breadth and level of complexity of accounting issues generally comparable to what can reasonably be expected to arise in the company’s financial statements, or experience actively supervising those engaged in such activities
• an understanding of internal control over financial reporting
• an understanding of the audit committee’s functions.

Questions for audit committees to consider

• Are audit committee members completing routine financial literacy self-assessments?
• Does the financial literacy self-assessment reflect recent developments?
• Are modifications to the committee’s education plan necessary?
• Are the audit committee’s training and education programmes designed to maintain financial literacy?

Director qualification disclosure requirements

King III proposes that the names and qualifications of the members of the audit committee be disclosed in the company’s integrated report. It is recommended that the disclosure should include information about the experience, qualifications, and attributes considered in the nomination process and the reasons why individuals should sit on the company’s board. Disclosures regarding individual board committee qualifications are required by King III, and companies may want to consider including the qualifications of the member as discussed during the committee selection process as a part of the overall board qualification disclosure.
Section 3

Key responsibilities
Audit committee charter and agenda

An annual review of the charter is recommended for all audit committees. Updates may be necessary as a result of:

- changes in regulatory or legal requirements
- the board’s delegation of new responsibilities to the audit committee or reassignment of certain responsibilities that are not required of the audit committee by law or regulation
- changes in the company’s Memorandum of Incorporation that affect the composition of the committee or how members are appointed
- identification of practices the committee wants to include among its responsibilities.

To help execute its role in a timely and efficient manner, the audit committee may use the responsibilities outlined in the charter to develop an annual calendar and meeting agendas. In addition to addressing responsibilities prescribed in the Companies Act, the charter should address the audit committee’s key recurring responsibilities as well as its responsibility for significant transactions and unusual events. The charter also should allow the committee to meet outside the official calendar when needed.

Concurrent with the charter review, the committee should examine its calendar of company activities and consider modifications based on the changes to the charter. The committee may also reconsider the frequency and timing of company’s activities already on the calendar.

In updating the charter and calendar, it may be helpful to consult with management, the internal auditors and the independent auditor. When appropriate, the committee should also seek legal counsel in reviewing its charter and the calendar.

Deloitte has developed a template to assist audit committees in drafting an appropriate charter. Best practice has been selected from a number of existing charters and relevant literature, such as the Companies Act and King III, has been considered. The template, which is reflected as Appendix A, may be used with the calendar planning tool in Appendix B.

The Companies Act and King III are silent on the requirements pertaining to the audit committee charter. However, the King Committee issued a Practice Note specifically dealing with the terms of reference of the audit committee.
When reviewing the audit committee charter, care should be taken to include the duties of the audit committee as prescribed in the Companies Act, the JSE listings requirements (for listed companies), and King III.

The legislated duties of the audit committee, as set out in the Companies Act, are:

- nominating an auditor that the audit committee regards as independent
- determining the audit fee
- ensuring that the appointment of the auditor complies with the Companies Act and other relevant legislation
- determining the nature and extent of non-audit services
- pre-approving any proposed agreement with the auditor for the provision of non-audit services
- preparing a report to be included in the annual financial statements describing how the committee carried out its functions, stating whether the auditor was independent, and commenting on the financial statements, accounting practices and internal financial control measures of the company
- receiving and dealing with relevant complaints
- making submissions to the board regarding the company’s accounting policies, financial controls, records and reporting, and
- any other function designated by the board.

Since the Companies Act prescribes the appointment process, composition and functions of the audit committee, it can now be described as a statutory committee. The audit committee will bear sole responsibility for its decisions pertaining to the appointment, fees and terms of engagement of the auditor. On all other matters it remains accountable to the board and, as such, it will function as a board committee.

The audit committee is obliged to report to shareholders by including in the annual financial statements a report describing how the audit committee carried out its functions, stating whether the auditor was independent, and commenting on the financial statements, accounting practices and internal financial control measures of the company.

In terms of the JSE listings requirements the audit committee is required to set a policy with regard to non-audit services provided by the independent auditor, and consider, on an annual basis, the appropriateness of the expertise and experience of the financial director. A statement to this effect must be included in the company’s integrated report.
In addition to the legislative duties set out in the Companies Act, and the considerations of the JSE listings requirements, King III proposes a number of additional functions, including:

- oversight of the internal audit function
- playing a key role in the risk management process and performing oversight of financial risks and reporting, internal financial controls and fraud and IT risks as they relate to financial reporting
- ensuring that a combined assurance model is applied to provide a coordinated approach to all assurance provided on company activities (in terms of this model, assurance should be done on three levels, i.e. management, internal assurance providers and external assurance providers)
- satisfying itself with regard to the expertise, resources and experience of the finance function
- oversight of the external audit process, and
- oversight of integrated reporting.

Assessment of the finance function

King III requires the audit committee to satisfy itself of the expertise, resources and experience of the company’s finance function. This entails an annual consideration of the appropriateness of the expertise and adequacy of resources of the finance function and experience of the senior members of management responsible for the financial function. The results of this assessment should be disclosed in the integrated report.

In addition, the JSE listings requirements requires the audit committee to evaluate the suitability of the expertise and experience of the finance director and recommend to the board if any changes are necessary.
The following inquiry may assist the audit committee in their assessment of the required resources in the finance function:
• What is the total full-time-equivalent headcount utilised in the finance function?
• Estimate the allocation of total full-time-equivalent headcount between:
  - Manager
  - Non-management/Temporary/Contractor
• Estimate the allocation of the total process cost (personnel cost plus outsourcing cost)
• Obtain the following for Transaction Processing volumes:
  - Number of active suppliers
  - Number of vendor invoices processed
  - Number of vendor invoices processed in a Shared Service Center
  - Number of customer remittances
  - Number of customer remittances automatically posted
  - Number of expense reports processed
  - Cycle time – elapsed business days from submission to delivery of payment of expense report
  - Number of customer invoices
  - Customer invoices generated manually
• Obtain of the following for General Accounting/Financial Reporting:
  - Number of General Ledger systems and respective complexities
  - Number of manual General Ledger journal entries
• Obtain a listing for the following Internal Controls within the finance function:
  - Total number of key controls
  - Number of automated key controls
  - External audit fees
• To what degree is business planning conducted through an automated planning tool?
• List the following for the Financial Management Reporting process.
  - Number of ad hoc Financial Management Reports created for each reporting cycle.
  - Number of standard Financial Management Reports created for each reporting cycle.
• To what the degree are Key Performance Indicators (KPIs) in Management Reporting linked to drivers of those indicators (i.e. cause and effect understood by management)?
Once the audit committee has familiarised itself with the required size and resources of the finance function, it may proceed to evaluate the structure, culture, expertise and effectiveness and the finance function.

- Does management of the finance function demonstrate a commitment to character, integrity and high ethical values through its attitudes and actions?
- Does management of the finance function demonstrate a commitment to competence? Is the level of competence required for particular jobs specified and translated into knowledge and skills?
- Are human resource policies and procedures properly developed and communicated to staff in the finance function regarding expected levels of integrity, ethical behaviour and competence?
- Can the finance function’s management philosophy and operating style be considered to be consistent with a sound control environment?
- Is the organisational structure of the finance function appropriately designed to promote a sound control environment?
- Does the finance function assign authority and responsibility to provide a basis for accountability and control?
- Does management of the finance function properly apply accounting principles in preparation of the financial statements?
- Is there a process for identifying and responding to the changing information and communication needs?
- Can financial reporting and related application and information systems considered to be reliable?
- Is appropriate and necessary information obtained from and provided to management?
- Is there a process for identifying and responding to the changing information and communication needs of management?
- Has a ‘whistle blowing’ programme been established, and is management’s reaction monitored as it relates to financial reporting?
- Is there a process in terms of which management holds internal meetings to obtain feedback on whether control activities are operating effectively?
- Does management’s communication across and outside the entity reflect an attitude toward sound internal control?
- Does management address issues raised by others, specifically external communications, in order to maintain an effective control structure?
- Are self-assessments conducted to promote control awareness and accountability?
Interaction with management

The audit committee needs to cultivate a transparent and constructive relationship with management to develop a commitment to honesty and integrity, which in turn impacts the quality of financial reporting and the internal controls. Management’s willingness to communicate potentially significant issues relating to financial reporting and regulation, including matters relating to accounting policies and judgments and the internal controls over financial reporting, are heavily dependent on how open the relationship is between management and the audit committee. Disagreements between management and the audit committee are a potential signal of significant deficiencies in internal control, errors in the financial reporting process and fraud risks.

Interaction with the internal auditors

An effective relationship between the audit committee and the internal auditors is fundamental to the success of the internal audit function. It has become increasingly important for audit committees to assess whether the internal auditors are monitoring critical controls and identifying and addressing emerging risks. The specific expectations for internal audit functions vary by organisation, but should include, at least, the following elements:

• objectively monitor and report on the health of financial, operational, and compliance controls
• provide insight into the effectiveness of risk management
• offer guidance regarding effective governance
• become a catalyst for positive change in processes and controls
• deliver value to the audit committee, executives and management in the areas of controls, risk management and governance to assist in the audit committee’s assessment of the efficacy of programmes and procedures
• coordinate activities and share perspectives with the independent auditor.
In support of these objectives, audit committees should take several steps to facilitate a mutually beneficial relationship with the internal auditors:

- hold regular private sessions with the internal auditors
- be available when contacted by the chief audit executive (CAE), and facilitate open communication between the CAE and the audit committee
- engage in discussions regularly; make the reporting relationship a substantial and communicative one
- be responsible for the appointment, performance assessment and dismissal of the CAE or outsourced internal audit function
- actively participate in discussing goals and evaluating the performance of the CAE; these responsibilities should not be delegated solely to the CFO or CEO
- challenge the CAE and the internal audit department by setting high expectations, communicating those expectations clearly, and holding the department accountable for meeting them
- see that the internal auditors have appropriate stature and respect and are visibly supported by senior management throughout the organisation
- support the CAE, providing guidance if needed and assistance when he or she reports potential management lapses.

Questions for audit committees to consider

- Does internal audit have a clearly articulated strategy that is reviewed periodically and approved by the audit committee?
- Does internal audit have a clear set of performance expectations that are aligned with the success measures of the audit committee, and that are measured and reported to the audit committee?
- Does internal audit have a charter that is periodically reviewed and approved by the audit committee? Does internal audit operate in accordance with its charter?
- Is the internal audit plan aligned to the key risks of the organisation and other assurance activities? Is internal audit’s risk assessment process appropriately linked to the company’s enterprise risk management activities?
- In delivering the internal audit plan, is internal audit flexible and dynamic in promptly addressing new risks and the needs of the audit committee?
- Does internal audit organise or perform peer reviews or self-assessments of its performance and report the results to the audit committee?
- Is internal audit appropriately funded and staffed?
- Is internal audit staffed with the appropriate mix of professionals to achieve its objectives?
- Is internal audit sufficiently independent of management?
- Is the CAE respected as an adviser to the audit committee and management on emerging risks?
- Is internal audit highly regarded and respected in the organisation?
- Is the level of assurance provided by internal audit and its interaction with other assurance sources clear and appropriate for the audit committee?
- Does internal audit meet regularly with the independent auditors to discuss risk assessments, the scope of procedures, or opportunities to achieve greater efficiencies and effectiveness in the company’s audit services?
- Are issues identified and reported by internal audit appropriately highlighted to the audit committee, and is the progress toward effective completed management actions tracked and reported?
- Is internal audit timely and proactive in the conduct and reporting of issues and in addressing them with management?
- Are reports and other communications from internal audit to the audit committee of an appropriate standard and do they provide value?
Through effective communication, the audit committee can help the CAE fully understand and achieve what is expected of him or her. Several questions help assess the current or prospective CAE’s ability to perform at a consistently high level:

- Was the audit committee involved in selecting the CAE?
- Was the bar set high enough to select the calibre of candidate needed?
- Does the audit committee have reasonable and appropriate expectations?
- Does the CAE have the right mix of experience and capabilities, including industry knowledge and business acumen, to understand the company’s risks?
- Does the CAE have a professional certification, such as certified internal auditor, and participate in relevant continuing education programs?
- Does the internal audit function have a quality improvement program?

When the internal audit function’s direct reporting line is to the audit committee, it allows the internal auditors to remain structurally separate from management and enhances objectivity. This also encourages the free flow of communication on issues and promotes direct feedback from the audit committee on the performance of the CAE. There are several ways the audit committee can oversee the internal audit function. The Institute of Internal Auditors (IIA) provides the following checklist of considerations for audit committees in overseeing the internal auditors.

**IIA Ten-point checklist for internal audit oversight**

1. The audit committee engages in an open, transparent relationship with the CAE.
2. The audit committee reviews and approves the internal audit charter annually.
3. The audit committee has a clear understanding of the strengths and weaknesses of the organisation’s internal control and risk management systems.
4. The approved plan is carried out by competent, objective professionals from internal audit.
5. Internal audit is empowered to be independent by its appropriate reporting relationship.
6. The audit committee addresses with the CAE all issues related to independence and objectivity.
7. Internal audit is quality-oriented and has a robust quality improvement program.
8. The audit committee regularly communicates with the CAE about performance and improvement opportunities.
9. Internal audit reports are actionable and recommendations are implemented.
10. The audit committee meets periodically with the CAE without management.
Internal audit oversights

The audit committee charter must include oversight of the internal audit function as one of its purposes. The audit committee’s regular report to the board of directors should include issues involving the performance of the internal audit function. The audit committee must meet separately with the internal auditors.

The audit committee oversees the accounting and financial reporting processes of the company. Note that oversight of internal audit is often one component in meeting this requirement.

In addition to the suggestions above, the audit committee should review and periodically evaluate the status of the enterprise-wide risk assessment and the audit plans. The audit committee also should periodically evaluate the progress and results of the audit against the original plans and any significant changes made to those plans.

The IIA’s Standards for Professional Practice of Internal Auditing mandate that the internal auditors maintain a certain level of independence from the work they audit.

This means that an internal auditor should have no personal or professional involvement with the area being audited and should maintain an impartial perspective on all engagements. Internal auditors should have access to records and personnel when necessary, and they should be allowed to employ appropriate investigative techniques without impediment.

Risk assessment and oversight

Risk oversight has taken on increased importance not only for audit committees, but for full boards. Many boards are reconsidering the risk governance structure and which committees have the expertise to oversee particular risks.

King III requires the board to exercise leadership and to ensure the governance of risk through a formal process. Although the board may delegate the responsibility of risk management to a board committee, it remains ultimately responsible. The board should be clear on its role in risk oversight. Examples include whether the entire board is involved or whether risk oversight is executed by a particular committee, and whether the employees responsible for risk management report directly to the board.
Risk oversight is a key responsibility of the board, and disclosure of its role will improve investors’ and shareholders’ understanding of this role.

Audit committees are responsible for financial risks and for overseeing the process for identifying and addressing those risks. However, the responsibility for other risks can be delegated to other board committees that have the appropriate expertise; for example, human resource and compensation risks can be overseen by the remuneration committee. Nonetheless, the full board has the ultimate responsibility for risk oversight and should discuss the organisation’s most material risks regularly.

The audit committee should discuss the company’s risk assessment and risk management policies with management. Although it is the responsibility of senior management to assess and manage the company’s risks, the audit committee should focus on areas of major financial risk exposure and discuss the guidelines and policies for addressing these areas. Consequently, risk oversight has been on the agenda of audit committees for a number of years. King III proposes that the audit committee should have an understanding of the company’s process for identifying, managing and reporting on risk.

At a minimum, the audit committee should ensure oversight of:

- financial reporting risks
- internal financial controls
- fraud risk as it relates to financial reporting, and
- IT risks as it relates to financial reporting.

Deloitte has identified six distinct areas of focus for the full board in helping to enable a risk-intelligent governance approach:

1. Define the board’s risk oversight role.
2. Foster a risk-intelligent organisational culture.
3. Help management incorporate risk intelligence into its organisational strategy.
4. Help define the risk appetite.
5. Execute a risk-intelligent governance process.
6. Benchmark and evaluate the governance process.
Questions for audit committees to consider

When the audit committee is considering the effectiveness of the company’s enterprise risk management - the process of planning, organising, leading, and controlling activities to minimise the effect of downside risk on the organisation - they may consider asking the following questions:

- What are the company’s policies and processes for assessing and managing major financial risk exposures on an integrated, enterprise-wide basis?
- What are the key risks, vulnerabilities, and plans to address them?
- Has the company defined its risk appetite with the board’s input and approval?
- How capable is the company of preparing for, responding to, and recovering from major financial risk exposures?
- How do our various board committees oversee risk? Is there appropriate coordination and communication?
- Is the full board participating in risk oversight and discussing the most material risks and how they are being monitored?
- Does the board consider the relationship between strategy and risk?
- Are we getting the information we need across the organisation for key decisions?
- Does the scenario planning include both individual and aggregate risk views?
- What mechanisms does management use to monitor emerging risks? What are the early warning mechanisms, and how effective are they? How, and how often, are they calibrated?
- Which framework has management selected for the risk management program? What criteria were used to select it?
- What is the role of technology in the risk management program? How was it chosen, and when was it last evaluated?
- What is the role of the tax department in the risk management programme? Are we taking steps to gain a high-level understanding not only of tax risk, but also of the benefits a robust tax risk management programme can offer?
Nine fundamental principles of a risk intelligence program

1. A common definition of risk addressing both value preservation and value creation is used consistently throughout the organisation.
2. A common risk framework supported by appropriate standards is used throughout the organisation to manage risks.
3. Key roles, responsibilities, and authority related to risk management are clearly defined and delineated.
4. A common risk management infrastructure is used to support the business units and functions in their risk responsibilities.
5. Governing bodies such as boards and audit committees have appropriate transparency and visibility into the organisation’s risk management practices.
6. Executive management has primary responsibility for designing, implementing, and maintaining an effective risk program.
7. Business units are responsible for their business and the management of risks they take within the risk framework established by executive management.
8. Certain functions (e.g., finance, legal, information technology, human resources) have a pervasive impact on the business and support the business units in the organisation’s risk program.
9. Certain functions (e.g., internal audit, risk management, compliance) monitor and report on the effectiveness of an organisation’s risk program to governing bodies and executive management.

Leading practices

- Increase the focus on risk oversight in board and committee agendas, particularly in the current economic environment.
- Develop a culture where risk is considered in decisions at all levels.
- Periodically reassess the list of most significant risks, determining the management members and board committees responsible for each.
- Given the importance of information technology to most organisations, focus on IT milestones and reporting against them, especially in respect of IT transformation.
- Review acquisitions, how they align with the defined risk appetite, relevant integration milestones, return on investment, and risk scenario planning, including risks associated with value creation and preservation.
- Have each business unit leader make a presentation at a board or audit committee meeting to enhance the members’ understanding of the business and risks and to reinforce that the business unit leaders are primarily responsible for effective risk management.
Combined assurance

King III specifies that the audit committee should ensure that a combined assurance model is applied to provide a coordinated approach to all assurance activities.

King III defines combined assurance as “integrating and aligning assurance processes in a company to maximise risk and governance oversight and control efficiencies, and optimise overall assurance to the audit and risk committee, considering the company’s risk appetite”.

Combined assurance is a concept that has been around for a while yet remains an area that a lot of organisations have not yet fully implemented. The contributing factors include the dynamic nature of the risk environment, the reliance on external assurance providers in directing assurance scope and the model needs to operate across business processes.

In adopting the combined assurance process an entity should adopt the appropriate approach in developing, designing and implementing the model. We have developed the Deloitte combined assurance framework to assist in assessing companies’ assurance practices and guide the development of an appropriate framework.

The Deloitte combined assurance framework consists of seven components. These seven components form the basis upon which a combined assurance programme and framework is assessed and benchmarked.
**Strategy Setting and Governance:** The first assessment component is to determine how the combined assurance model has been designed to support the organisation’s strategy setting and governance processes. As risk management is an integral part of understanding and determining the strategic direction of the organisation, similarly combined assurance needs to be aligned with the strategic direction, risk and objectives of the entity.

In addition, combined assurance is the apex upon which the organisation’s governance turns, including the tone at the top, the culture, risk appetite, control environment and assurance regime.

In developing the combined assurance policy the relationship between strategy, risk and combined assurance should be clearly defined. The role of the audit committee for ensuring the design and implementation of a combined assurance model/framework should be highlighted in the policy.

**Compliance, risk and control frameworks:** The frameworks defined within an organisation may include compliance, governance, risk and control frameworks. These frameworks are developed in line with best practice standards and guidelines such as COSO, ISO and CoBIT.

With the development of a combined assurance framework the interplay and interdependencies within the other governance frameworks need to be clearly articulated and defined. This includes defining elements such as oversight, roles and responsibilities, reporting requirements and integrated assurance plans.

**Scoping and planning:** A critical element of combined assurance is the understanding of your environment, setting your risk appetite and defining the specific scope in order to achieve the desired level of comfort from your combined assurance model.

Within the planning stages it is important to map the key risks, the defined levels of assurance and how this practically translates into your organisation’s first, second and third lines of defence. Once the risk and assurance mapping has taken place the level of residual exposure should be agreed upon with the audit committee.

The planning stage also needs to identify the key stakeholders. The different types and level of assurance should be defined and included in the combined assurance framework.

Clearly defined roles and responsibilities need to be defined and understood within the organisation as combined assurance is not one unit’s responsibilities but cuts across all areas within your business.
The level of contribution and the critical success of implementation are dependent on clearly defined roles and responsibilities.

**Coordination:** Coordination with both internal and external parties is vital to the success of a combined assurance programme. Within the defined levels of assurance the audit committee needs to ensure coordination of assurance from management through to external assurance providers. The level of consultation will differ across the assurance spectrum due to the risk exposure, assurance coverage and the nature of the assurance.

**Reporting:** Having combined assurance in place will help to ensure that the audit committee has the information they need, in order to make an accurate assessment. This provides stakeholders with more comfort and the confidence that management can achieve its objectives and prevent hazards from materially damaging the business.

The combined assurance pyramid ensures that the right information is measured and gathered by the right people in the first layer. The data is refined in the second and passed on to the top of the pyramid to the directors, managers and audit committee members in a readily digested form.

As a consequence of the measurable benefits that flow from effective combined assurance, organisations that opt for compliance will enjoy a competitive edge that their less nimble peers will eventually be forced to follow.
**Technology:** Most business processes in today’s world are supported by technology. The audit committee should ensure that combined assurance is appropriately supported with the correct infrastructure, tools and technology. The level of support may differ depending on the level of maturity. The support requirements and needs to your combined assurance model will be assessed and recommendations made where necessary.

An example of a technology used to support combined assurance is the management control self-assessment tool.

**Fraud and internal control over financial reporting**

In conjunction with risk oversight, the audit committee should determine that the company has programmes and policies in place to prevent and identify fraud. It should work with management to oversee the establishment of appropriate controls and antifraud programmes and to take the necessary steps when fraud is detected. The audit committee should also be satisfied that the organisation has established a complaint hotline. See the Complaint Hotline Procedures section later in the document for more information.

Audit committee members should be aware of three main areas of fraud:

- financial statement fraud, which includes intentional misstatements in or omissions from financial statements
- asset misappropriation, which may include forgery, theft of money, inventory theft, payroll fraud, or theft of services
- corruption, which may include schemes such as kickbacks, shell companies, bribes to influence decision-makers, or manipulation of contracts.

Although the audit committee should be concerned with all three types of fraud, financial statement fraud should be their primary focus. Although it occurs least frequently, it is often the most costly.

One way the audit committee can help in overseeing the prevention and detection of financial statement fraud is by monitoring management’s assessment of internal control over financial reporting. To oversee internal control over financial reporting successfully, the audit committee must be familiar with the processes and controls that management has put in place and understand whether they were designed effectively. The audit committee should work with management, the internal auditors, and the independent auditor to gain the knowledge needed to provide appropriate oversight.
The audit committee should also have an awareness of the following Acts:
• Prevention and Combating of Corrupt Activities Act
• Financial Intelligence Centre Act
• Prevention of Organised Crime Act
• Protected Disclosures Act
• Electronic Communications and Transactions Act
• Promotion of Administrative Justice Act

The above list highlights those Acts which are relevant in South Africa. However, where the entity has operations in other countries, the laws and regulations of those countries should not be forgotten, for example the Foreign Corrupt Practices Act (United States).

The committee should understand the company’s responsibilities regarding these statutes as well as the policies and practices in place related to compliance with the statutes. The audit committee should also ask management what the company’s plans are should a violation occur, and it should be made aware of any actual violations, including management’s response.

**Leading practices for the oversight of financial reporting and internal controls include the following:**

• understand key controls and reporting risk areas as assessed by financial management, the internal auditors, and the independent auditor
• emphasise oversight of corporate taxes, an area where high-risk and high-dollar decisions are made
• leverage the value of internal controls beyond compliance
• consider levels of authority and responsibility in key areas, including pricing and contracts, acceptance of risk, commitments, and expenditures
• understand complex accounting and reporting areas and how management addresses them
• understand significant judgments and estimates used by management and their impact on the financial statements, such as fair-value accounting and related assumptions
• anticipate and understand how pending financial reporting and regulatory developments may affect the company, particularly its talent needs.
Complaint hotline procedures

Companies use hotlines to report a range of compliance issues, including violations of the internal policies of the business. A thorough, independent, and objective process should be established by management and the audit committee for investigating complaints. Companies use various procedures, but the most common method of receiving tips from inside and outside the organisation is through a telephone hotline administered by an internal department or a third party. Telephone hotlines have emerged as a preferred mechanism because they are interactive, allowing a skilled interviewer to elicit details.

Section 94 of the Companies Act requires the audit committee to receive and deal appropriately with any concerns or complaints, whether from within or outside the company, or on its own initiative, relating to:
• the accounting practices and internal audit of the company
• the content or audit of the company’s financial statements
• the internal financial controls of the company
• any related matter.

The audit committee should work with management to determine that more than one person in the company is aware of questions or complaints received from third-party vendors, in e-mail, or through other submission vehicles. Responsibility for investigating questions or concerns and reporting back to the audit committee often falls on individuals in the ethics and compliance, internal audit, legal, or risk management departments. Complaints should be categorised and analysed by root cause, and recommendations should be made to the audit committee on how to reduce the risk of similar complaints in the future.

The audit committee also should be provided with an on-going analysis of the progress of complaint resolution. Reports should be provided to the audit committee regularly in accordance with standing instructions. Some complaints may warrant immediate communication to the audit committee, such as those involving senior management and significant amounts. The audit committee should establish a schedule for reporting to the board of directors.
It is recommended that complaint hotline systems feature:
• operation by an independent third party
• staffing by trained interviewers rather than fully automated systems
• a dedicated phone number that is available at all times, along with other reporting means such as fax, the company’s web site, e-mail, and regular mail
• multilingual systems and operators.

In addition:
• complainants should be allowed to call back at a later time, and they should be given the option to file complaints anonymously
• complainants must be protected from any retaliation as a result of reporting
• protocols should be in place to allow complaints to be channelled to the appropriate individual, and complaints involving senior management should go directly to the audit committee
• complaints must be handled in a confidential manner and resolved as quickly as possible
• complaint procedures should be well known to all employees, vendors, and other interested parties.

A hotline monitored by an independent third party is preferred. However, if the hotline is administered internally, operators should have specific training on where to direct questions or complaints, including those related to human resources. Whatever the method, audit committee members should work with management to make employees, investors, and others aware of the option of confidential disclosure. Employees can be informed in the code of ethics, the employee handbook, human resources orientation, and ethics training. Instructions for submitting questions or complaints can be posted in company facilities and on intranet sites.

The company website is a natural vehicle for communicating the procedures to individuals outside the organisation. It is good practice for companies to adopt codes of ethics and disclose them on their websites. Information on the code of ethics and the complaint hotline often is linked from the home page under a section called “Ethics” or an equivalent.

Telephone operators working in customer service and investor relations should be prepared to answer questions on how to submit concerns and complaints regarding financial reporting.
It is important for the audit committee to work with management and internal audit to understand:
- opportunities to enhance internal whistleblowing systems
- the potential advantages of implementing timely internal whistle-blower cash awards to sustain and encourage internal whistleblowing
- the potential value of transaction monitoring tools to help promptly identify potential securities fraud issues such as bribery or financial statement fraud.

**Integrated reporting**

Following the incorporation of King III into the Johannesburg Stock Exchange Listing Requirements, listed companies are required to issue an integrated report for financial years starting on or after 1 March 2010, or explain why they are not doing so.

Good governance requires transparency and therefore we recommend that all organisations consider the principles of integrated reporting to understand how to best apply it in their specific circumstance. In particular we recommend that organisations better understand the impact the ever increasing focus on environmental and social matters will have on their upstream and downstream supply chain, to ensure that the opportunity to maximise competitive advantage is utilised.

It is important though to recognise that integrated reporting is a journey and reporting will improve over time.

The actual effective ownership by the board of the integrated reporting process, and the integrated report itself, is of significant practical importance. Based on our experience of working with our clients in this area over the last few years, it is one of the key determinants for a good integrated report.

There is indeed an important difference between the audit committee and the board actually setting and owning the agenda in this regard, or effectively acquiescing to an agenda set and populated by executive management or those that report to them and which is submitted to the board for approval, very often at a late stage of the process. Due to the evolving nature of development of integrated reporting and integrated reports, a greater degree of pro-activeness is indicated than is the case with the more traditional areas of responsibility, where more mature and generally-accepted frameworks are in place. This requires boards and audit committees to equip themselves properly in this area, and/or to seek the appropriate assistance to properly discharge their responsibilities.
According to King III, the board should ensure the integrity of the integrated report (Principle 2.12), and the audit committee should oversee integrated reporting (Principle 3.4). Detailed requirements for audit committees in King III, that directly and indirectly impact on the effective ownership of the integrated report include:

- the responsibility to consider whether an unbiased picture of the company’s position, performance or sustainability is being presented
- the responsibility for evaluating the significant judgments and reporting decisions affecting the integrated report
- the responsibility to understand how materiality for the integrated report has been determined, and
- the responsibility to ensure that forward-looking information provides a proper appreciation of the key drivers that will enable the achievement of such goals.

To discharge these responsibilities properly, as well as those set out in the Companies Act and contained in Corporate Law, the board should proactively set and own the integrated reporting agenda. In this regard, the view from executive management is obviously important to take into account in setting the agenda and framework, but once these are finalised by the board, the primary role of executive management and those that report to them is to operationalise and report back to the board within the framework thus established.

If, as is generally accepted, the integrated report indeed reflects the collective mind of the board and the integrated thinking that is essential for business in the modern world, a more reactive approach by the board would not effectively enable capturing the essential qualities and prerequisites for integrated reports.

In our opinion, the practical consequences of where the audit committee does not effectively own the integrated reporting process and the integrated report result in, amongst other things, the following shortcomings:

- an overly long report which does not achieve the key requirement of conciseness;
- a report without a clear and consistent storyline
- a report containing a volume of information that is clearly not material from the perspective of stakeholders, but which is included to accommodate internal political interests within the company
- a report where superficial and inadequate attention is paid to describing how the professed company values are actually lived and applied
- a report that does not display evidence of the necessary trade-offs and optimisation that is part and parcel of the modern business environment
• a report consisting of marketing-oriented material without adequate and consistent depth, and
• a report structure, format and content that may give a reader the impression that the oversight role of the board is not as strong as it properly should be.

The purpose of an integrated report is to tell the unique story of the company and the manner in which it sustains and adds value in the short, medium and long term. The board is clearly intended to bear the ultimate overall accountability for the company and its journey, and has been placed in a unique position to practically discharge this responsibility by a variety of formal and informal arrangements. In order to discharge this accountability effectively, the audit committee (on behalf of the board) should therefore also embrace the proactive and effective ownership of the integrated reporting process and the integrated report.

The International Integrated Reporting Council (IIRC) has developed a framework for an integrated report. The framework makes it clear that a principle based approach should be followed in the preparation of the integrated report. Rather than to provide a list of detailed disclosures, the framework sets the scene and provides the underlying principles and considerations that should guide the approach to integrated reporting and the publication of the integrated report.

In essence, the framework proposes that the company should explain to its stakeholders how it creates and sustains value in the short, medium and long term. The explanation should adhere to the fundamental concepts and guiding principles in describing the business model used to create value. In doing so, the company should discuss and link all content elements. This should all be underpinned by the strategic objectives of the business.

In addition, the framework explains:
• the concept of the six capitals (inputs or resources utilized by a company to create and store value)
• the need to describe the company’s business model and the manner in which this should be done, and
• the meaning of value created or destroyed by the company.

The IIRC framework makes it clear that any communication purporting to be an integrated report should comply with the minimum reporting standards identified in the framework.
Assurance of sustainability reporting and disclosure

King III (Principle 9.3) recommends that sustainability reporting and disclosure, or rather information other than financial information reported in the annual financial statements, should be independently assured. Assurance over the financial disclosure in the integrated report should be obtained. A formal process of assurance with regard to sustainability reporting should be established.

The Global Reporting Initiative (GRI) has designed and published a global sustainability reporting framework supplemented by sector specific guidelines. This voluntary framework with self-declaration of level of application is most commonly used in South Africa to guide sustainability disclosure. Application Levels range from C to A, with C indicating the minimum disclosure.

Some companies seek independent assurance over their Application Level. This is sourced from a variety of third party service providers and the assurance standard used and the type of assurance provided, vary.

There are two assurance standards that are generally used, namely the assurance standard issued by the International Federation of Accountants, ISAE 3000¹, and that issued by AccountAbility, AA 1000 AS. The levels of assurance provided by those two standards are depicted in the diagram below:

AA 1000 Assurance Standard (2008) vs ISAE 3000

<table>
<thead>
<tr>
<th>Standard</th>
<th>Level of assurance</th>
</tr>
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<tbody>
<tr>
<td>ISAE 3000</td>
<td>Limited</td>
</tr>
<tr>
<td>AA 1000 AS</td>
<td>Moderate</td>
</tr>
<tr>
<td></td>
<td>High</td>
</tr>
</tbody>
</table>

King III recommends that:
- ‘sustainability’ assurance is an on-going, integral part of the integrated reporting cycle
- ISAE 3000 and AA 1000 AS methodologies are used in combination to ensure the needs of the stakehold–ers and those of the company are met in a single process. In obtaining assurance, the company should be clear on the scope of the assurance to be provided and this should also be disclosed.

¹ International Standard on Assurance Engagements (ISAE) 3000, Assurance Engagements Other than Audits or Reviews of Historical Financial Information
General oversight and reporting disclosure should be delegated by the board to the audit committee. The audit committee should assist the board in reviewing the integrated report to ensure that the information is reliable and that it does not contradict the financial aspects of the report. The audit committee should also oversee the provision of assurance over sustainability issues in the same way that it would do with financial matters. For example, it would consider whether appropriate policies and processes are in place, whether they are adhered to, and whether the information about performance is reliable. This role of the audit committee is still necessary with regard to sustainability performance and reporting, even if there is a separate sustainability committee, or if sustainability matters are addressed by another board committee.
Questions for audit committees to consider in establishing a sound assurance regime

• What are the key business processes and/or information that need to be assured?
• Which of these key business processes and/or information will we need to make public representations about and when will this be feasible?
• Is the framework in terms of which representations of these processes and/or information are prepared acceptable and robust?
• Who are all the actual and potential parties who are relied upon to provide assurance and is a Combined Assurance Model being followed? Is the assurance process as efficient and effective as it can be? Where there are overlaps or gaps, are we satisfied that the risks warrant the continuation of such arrangements?
• Has a consistent and appropriate level of materiality been approved and accepted by the company for purposes of internal assurance providers? Are those levels of materiality compatible and defensible compared to those that will be used by external assurance providers?
• Are the criteria against which the subject matter(s) must be weighed in the assurance process reliable, neutral, understandable, complete and relevant?
• Are the standards which will be used by the parties providing assurance consistent and compatible? Are the levels of assurance to be provided consistent and compatible? Is there a requirement for rationalisation and improvement?
With respect to specific disclosures in the integrated report, King III requires that the following information relating to the functioning of the audit committee is provided in the integrated report:

• a summary of the role of the audit committee
• a statement on whether or not the audit committee has adopted a formal terms of reference that have been approved by the board and if so, whether the committee satisfied its responsibilities for the year in compliance with its terms of reference
• the names and qualifications of all members of the audit committee during the period under review, and the period for which they served on the committee
• the number of audit committee meetings held during the period under review and members’ attendance at these meetings
• a statement on whether or not the audit committee considered and recommended the internal audit charter for approval by the board
• a description of the working relationship with the CAE
• information about any other responsibilities assigned to the audit committee by the board
• a statement on whether the audit committee complied with its legal, regulatory or other responsibilities, and
• a statement on whether or not the audit committee recommended the integrated report to the board for approval.

It is important that full disclosure of the activities of audit committee is communicated to the user, as it impacts the users’ perceptions of the involvement of the audit committee, and how the audit committee has fulfilled their responsibilities.
Interaction with the independent auditor
Audit committees of companies are directly responsible for the appointment, compensation, and oversight of the independent auditor, including the resolution of any disagreements with management. It is optimal that the audit committee, management, the internal auditors, and the independent auditor work together in a spirit of mutual respect and cooperation. The active involvement of a high-quality, transparent audit committee will enhance the perception of the audit quality and of the quality of the financial statements.

Leading practices for the audit committee’s relationship with the independent auditor include:

- exercise ownership of the relationship with the independent auditor
- discuss with the auditor any potential or contentious issues in terms of independence/ethical requirements
- get to know the lead partners and meet periodically with specialists (e.g., tax, IT, fair value)
- establish expectations regarding the nature and method of communication, as well as the exchange of insights
- engage in consistent dialogue outside of the regularly scheduled meetings
- set an annual agenda with the independent auditor
- focus on independence, including a process for the preapproval of services beyond the audit
- provide formal evaluations and regular feedback.

Private sessions with the independent auditor are a way to maintain open communication and identify concerns. The audit committee and the independent auditor typically meet at least quarterly and engage in thorough discussion.

The audit committee should have a process for overseeing management’s resolution of significant issues raised by the independent auditor.
Communication between the audit committee and the independent auditor

The independent auditor is required by the International Standards on Auditing to communicate the following to the audit committee:

- the auditor’s responsibilities in relation to the audit. This may include an understanding of the terms of the audit engagement, normally outlined annually in an engagement letter, including the objective of the audit and the responsibilities of the auditor and management
- the form, timing and expected general content of communications with the audit committee
- an overview of the planned scope and timing of the audit. This may include:
  - the nature and extent of specialised skills necessary to perform planned audit procedures
  - the extent to which the independent auditor plans to rely on work performed by the company’s internal audit function or others in the audit of the financial statements and internal control over financial reporting
  - the names, locations, and anticipated responsibilities of any firm or personnel performing audit work in the current period but not employed by the auditor
- the auditor’s rationale for serving as principal auditor if significant parts of the work are performed by others, and
- any significant changes to the original strategy or significant risks and the reasons for such changes
- fraud or information that indicates that fraud may exist or other matters relating to fraud relevant to the responsibilities of the audit committee
- suspected or actual non-compliance with laws and regulations
- significant findings from the audit and the auditor’s views about significant qualitative aspects of the entity’s accounting practices, including accounting policies, accounting estimates and financial statement disclosures.

Matters to be discussed may include:

- management’s initial selection of, or changes in, significant accounting policies or the application of such policies in the current period, and
- the effect on financial statements or disclosures of significant accounting policies in controversial areas or areas for which there is a lack of authoritative guidance or consensus, or diversity in practice
- all critical accounting policies and practices to be used, including (i) the reasons certain policies and practices are considered critical, and (ii) how current and anticipated events might affect the determination of whether certain policies and practices are considered critical
- when applicable, an explanation of why the auditor considers a significant accounting practice, that is acceptable under the applicable financial reporting framework, not to be most appropriate to the particular circumstances of the entity
- critical accounting estimates, including (i) a description of the process management used to develop critical accounting estimates, (ii) management’s significant assumptions used in critical accounting estimates that have a high degree of subjectivity, (iii) any significant changes management made to the processes used to develop critical accounting estimates or significant assumptions, a description of management’s reasons for the changes, and the effects of the changes on the financial statements
- significant unusual transactions, including (i) significant transactions that are outside the normal course of business for the company or that otherwise appear to be unusual due to their timing, size, or nature, and (ii) the policies and practices management used to account for significant unusual transactions
- significant matters arising during the audit in connection with related parties
- material misstatements of fact contained in other information. The auditor may also communicate their responsibility, including any related procedures performed and the results of such procedures when other information is presented in documents containing audited financial statements
- events or conditions which cast significant doubt on the entity’s ability to continue as a going concern. The communication may include the auditor’s conclusion about management’s plans to alleviate substantial doubt about the company’s ability to continue as a going concern and the effects, if any, on the financial statements and the auditor’s report, if substantial doubt remains about the company’s ability to continue as a going concern
- uncorrected misstatements and the effect that they may have on the opinion in the auditor’s report and the effect of uncorrected misstatements related to prior periods, including those were there was another predecessor auditor, on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole
- other matters communicated or discussed with management
- written representations the auditor is requesting
• possible modifications to the auditor’s report
  i.e. a modified opinion or an emphasis of
  matter or other matter paragraph, including
  the reasons for modifying the opinion and the
  proposed wording to be used in the auditor’s
  report
• any significant difficulties encountered
  during the audit, including, but not limited
  to, (i) significant delays by management, the
  unavailability of company personnel, or an
  unwillingness by management to provide
  information needed for the auditor to perform
  his or her audit procedures, (ii) an unreasonably
  brief time within which to complete the audit,
  (iii) unexpected extensive effort required by
  the auditor to obtain sufficient appropriate
  audit evidence, (iv) unreasonable management
  restrictions encountered by the auditor on the
  conduct of the audit, and (v) management’s
  unwillingness to make or extend its assessment
  of the company’s ability to continue as a going
  concern when requested by the auditor
• significant deficiencies in internal control
  identified during the audit, including a
  description of the deficiencies and an
  explanation of their potential effects. This
  would also include significant deficiencies
  identified by component auditors
• group audit matters i.e. scope of the audit,
  involvement in the component auditor’s work,
  limitations on the scope of the work, fraud
  related matters
• failures by group management to inform
  component management of matters significant
  to the financial statements of the component
• matters relating to subsequent events i.e. facts
  discovered after the date of the auditor’s report
  but before the financial statements are issued
  that would have impacted the auditor’s report
  or are discovered after the financial statements
  have been issued
• other matters arising from the audit that are
  significant to the oversight of the company’s
  financial reporting process, including
  complaints or concerns regarding accounting
  or auditing matters that have come to the
  auditor’s attention during the audit and the
  results of the auditor’s procedures regarding
  such matters
• certain matters relating to the auditor’s
  independence.
In addition, the independent auditor generally communicates the following to the audit committee:

• whether the audit committee is aware of matters relevant to the audit, including, but not limited to, violations of laws or regulations
• matters that are difficult or contentious for which the auditor consulted outside the engagement team and that the auditor reasonably determined are relevant to the audit committee’s oversight of the financial reporting process
• management’s consultation with other accountants about significant auditing or accounting matters when the auditor has identified a concern regarding such matters
• any disagreements with management about matters, whether or not satisfactorily resolved, that individually or in the aggregate could be significant to the company’s financial statements or the auditor’s report.

Audit committee to communicate with the independent auditor

• Meet to review and discuss with the independent auditor the company’s annual audited financial statements and quarterly financial statements, including disclosures in management’s discussion and analysis
• Periodically, meet separately with the independent auditor, management, and the internal auditors
• Obtain a formal written communication from the independent auditor regarding independence and other matters annually
• Review with the independent auditor any audit problems or difficulties and management’s response
• Set clear hiring policies for employees or former employees of the company’s independent auditor.
• Review the scope and the extent of non-audit services provided (and pre-approved) with the independent auditor.
• Discuss and agree the audit fee with the independant auditor.
Auditor Independence

Independence is governed primarily by the requirements of section 290 of the International Ethics Standards Board for Accountants (IESBA) Code of Ethics for Professional Accountants (the IFAC Code). Furthermore, auditors are required to comply with the Independent Regulatory Board for Auditors (IRBA) Code of Professional Conduct for Registered Auditors, which is similar to the IFAC Code.

Locally, the Companies Act and King III provide guidance to ensure that the auditor’s independence is guaranteed. These rules recognise the critical role of audit committees in financial reporting and their unique position in monitoring auditor independence. The Companies Act makes it clear that the audit committee’s main responsibility is to ensure that the auditor is, and remains independent. As such the appointment of the auditor is dependent on the audit committee’s confirmation that the auditor is independent of the company.

The Companies Act sets out the duties of the audit committee. The majority of the statutory duties are aimed at ensuring that the independent auditor is and remains independent. Cognisance should be taken of the provisions of section 90(2) and (3) of the Companies Act in which requirements for the appointment of the auditor is set out. Both the person responsible for the audit as well as the audit firm are prohibited from providing accounting, book-keeping and related secretarial services on a regular or habitual basis, and may not engage for more than one year in the maintenance of any of the company’s financial records or the preparation of any of its financial statements. Where such services were provided at any time in the five years preceding the appointment of the auditor, such auditor will be disqualified from appointment. In this regard, it should be noted that the Regulatory Board for Independent Auditors (IRBA) and the Companies and Intellectual Property Commission (CIPC) enforce the said provisions from 1 January 2014 on a prospective basis, i.e. they only consider the services listed in section 90(2) rendered after 1 January 2014.
Audit committee’s statutory duties to ensure the independence of the independent auditor

Section 94(7) of the Companies Act

An audit committee of a company has the following duties:
(a) To nominate, for appointment as auditor of the company under section 90, a registered auditor who, in the opinion of the audit committee, is independent of the company;
(b) to determine the fees to be paid to the auditor and the auditor’s terms of engagement;
(c) to ensure that the appointment of the auditor complies with the provisions of this Act and any other legislation relating to the appointment of auditors;
(d) to determine, subject to the provisions of this Chapter, the nature and extent of any non-audit services that the auditor may provide to the company, or that the auditor must not provide to the company, or a related company;
(e) to preapprove any proposed agreement with the auditor for the provision of non-audit services to the company;
(f) to prepare a report, to be included in the annual financial statements for that financial year—
   (i) describing how the audit committee carried out its functions;
   (ii) stating whether the audit committee is satisfied that the auditor was independent of the company; and
   (iii) commenting in any way the committee considers appropriate on the financial statements, the accounting practices and the internal financial control of the company;
(g) to receive and deal appropriately with any concerns or complaints, whether from within or outside the company, or on its own initiative, relating to—
   (i) the accounting practices and internal audit of the company;
   (ii) the content or auditing of the company’s financial statements;
   (iii) the internal financial controls of the company; or
   (iv) any related matter;
(h) to make submissions to the board on any matter concerning the company’s accounting policies, financial control, records and reporting; and
(i) to perform such other oversight functions as may be determined by the board.
Assessment of independence

Section 94(8) of the Companies Act

In considering whether, for the purposes of this Part, a registered auditor is independent of a company, the audit committee of that company must—
(a) ascertain that the auditor does not receive any direct or indirect remuneration or other benefit from the company, except—
   (i) as auditor; or
   (ii) for rendering other services to the company, to the extent permitted in terms of subsection (7) (d);
(b) consider whether the auditor’s independence may have been prejudiced—
   (i) as a result of any previous appointment as auditor; or
   (ii) having regard to the extent of any consultancy, advisory or other work undertaken by the auditor for the company
(c) consider compliance with other criteria relating to independence or conflict of interest as prescribed by the Independent Regulatory Board for Auditors established by the Auditing Profession Act, in relation to the company, and if the company is a member of a group of companies, any other company within that group.
The independence rules are different for entities governed by the Securities Exchange Commission (SEC). For such entities the SEC rules should be studied on what is applicable.

For the purpose of this section, we will focus on the independence principles per the IFAC code. The independence rules address the following issues:

• relationships between the auditor and its audit client arising from:
  - personal financial interests
  - family and personal relationships
  - employment relationships
  - business relationships with audit clients and consultants
• non-assurance services provided by auditors
• contingent fees and commissions
• long association of senior personnel with the audit client, which incorporates partner rotation
• the audit committee’s administration of the audit engagement
• compensation of audit partners

**Financial interests.** Holding a financial interest in an audit client may create a threat to independence depending on the (a) role of the person, (b) whether the holding is direct or indirect and (c) the materiality of the financial interest. Examples of such threats can include investment in the audit client’s debt or equity securities, loans, collective investment funds and other financial interest products, or financial interests held by trusts or estates of which certain of its people (and or their immediate family members) are trustees or executors. (In some audit firms the rules regarding investments in audit clients can be more restrictive than the IFAC rules and the audit committee should enquire from the auditor if they have more restrictive policies on financial interest).

**Family and personal relationships.** Threats to independence occur when family and personal relationships exist between the audit team and a director or officer or certain employees (depending on their role) of the audit client. Depending on the closeness of the relationship safeguards could reduce the threat to an acceptable level otherwise the individual who has such a relationship shall not be a member of the audit team.
**Employment relationships.** The rule states that independence is impaired if a current partner, principal, shareholder, or professional employee of the independent auditor has an employment relationship with, or serves as a member of the board of directors or similar management or governing body of, the audit client.

Independence can be impaired if former partners or members of the audit engagement team are employed as directors or officers or employees in positions to exert significant influence over the preparation of the audit client’s accounting records of the financial statements on which the audit firm express an opinion on. Such individuals should not be employed by the audit client unless certain criteria are met such as the position offered to the person, the former role of the person as the audit client, continuous involvement at the audit client and the time that has passed from last audit prior to position being filled.

Partners of the audit firm should not act temporarily as a director, officer or employee of an audit client. Lending of professional staff to an audit client for a short period of time may in certain instances be provided. The temporary lending of staff is not allowed for audit clients that are SEC Registrants or affiliates of SEC Registrants.

**Business relationships.** The rule prohibits an independent auditor from having a direct or material indirect business relationship with an audit client, or with persons associated with the audit client in a decision-making capacity, such as an audit client’s officers, directors, or substantial stockholders. This prohibition does not preclude the independent auditor from providing permissible services to the audit client or purchasing goods or services from the audit client as a consumer in the ordinary course of business.

There are rules for different types of business relationships between the audit firm and the audit client or its personnel that should be considered. For example:

- **Vendor Business Relationships**
- **Marketplace Business Relationships** (including, Alliances, Teaming, prime / subcontracting, reseller, investment, commission or referral fee, sponsorships, co-publishing and speaking engagements.)
Non-assurance services provided by auditors. Providing non-audit services to the audit client may create threats to independence. The rules permit an auditor to provide certain non-audit services and in other cases it may be possible to eliminate or reduce the threats created by the application of safeguards. Non-audit services are required to be preapproved by the audit committee; The terms “audit” or “audit services” would bear the same meaning as elsewhere in the Companies Act or the statute which requires the appointment of an auditor. The exact extent of “audit services” is not entirely clear. In the event that the auditor intends to perform services for the company of which their inclusion in the meaning of “audit services” could be contentious, the auditor should clearly set out such services in a document and obtain preapproval from the audit committee for the performance of such services, prior to the conclusion of a formal contract with the company in this regard. This situation would typically arise where a company, as a matter of policy, imposes certain procedures on itself which are not strictly speaking required as part of the audit.

The phrase “audit services” would refer to those activities performed under the supervision and direction of the auditor in order to support an opinion on the annual financial statements, a review opinion on interim financial information, and, where applicable, other matters which are consequential on the audit appointment and which arise from statute (for example, the capital adequacy (Basel II) reports issued by an auditor of a registered bank in terms of the Banks Act).

As the audit committee determines the audit fee and terms thereof; and also the nature and extent of any non-audit services, and as both are ordinarily the subject of an engagement letter, there should be little risk arising from the definition as, whether the auditor includes a service as an audit service or a non-audit service, the audit committee would have input in approving such a service.

The interpretation of the phrase “pre-approve any proposed contract with the auditor for the provision of non-audit services to the company” is difficult. However, it is important to consider both the intent of the legislation and also other practice in markets which have similar provisions.
On this basis it is possible for there to be a master service agreement in place governing the auditor’s provision of non-audit services, provided the agreement includes all material terms governing the provision of such non-audit services. Where an auditor has such pre-approval in place it would nonetheless be incumbent on the auditor to table for approval from time to time the extent of fees to be paid or paid in respect of actual non-audit services provided. Further, the master service agreement should include the terms under which the services are provided, the nature of services which can be provided, and the extent of such services, which is pre-approved by the audit committee. If services are provided under different terms to those pre-approved by the audit committee, then these terms should be pre-approved by the audit committee.

A pre-approval policy drafted by the audit committee will not be sufficient to discharge the obligation on the audit committee to pre-approve all non-audit services. The provisions of section 94(7)(d) that the audit committee must determine the “nature and extent” of any non-audit services to be provided by the auditor appear, however, to require that the audit committee formulates a policy in this regard. Amongst other things, the audit committee could consider a list of services which the auditor would not, as a matter of principle, be allowed to render or certain limitations on fees to be paid for non-audit services received from the auditors.

The auditor should never take up a management responsibility when providing any permissible non-audit services to the audit client.

The independence rules include certain prohibitions on the following list of services depending if the non-audit services is being provided to the audit client, or any of its subsidiaries, affiliates or divisions. Some of the non-audit services are completely prohibited for public interest entities.

List of non-audit services with specific independence rules to be considered include:

- tax services as follows:
  - tax return preparation services
  - tax calculations for purpose of preparing the accounting entries
  - tax planning and other tax advisory services
  - assistance in resolution of tax disputes
- design and implementation of financial information systems
- appraisal or valuation services, fairness opinions, or contribution-in-kind reports
- actuarial services
- internal audit services
- human resources (including recruiting senior management)
- corporate finance services (including broker-dealer, investment advisory, or investment banking services)
- legal services
- litigation support and expert services
- bookkeeping
- temporary staff assignments
Useful tips when considering auditor independence

This is not a comprehensive list, but can be used when dealing with the auditor on various aspects:

• obtain confirmation from the auditor on the audit team’s independence in respect of financial interests of both the team members and their immediate family members
• consider independence prior to offering a position to a member of the audit team and communicate this to the audit partner in time
• consider the list of prohibited services when requesting services from the auditor
• the audit team should never act in a capacity of management / perform a management function when providing permissible non-audit services to the audit client
• temporary staff placements from the audit team, are not in all instances possible
• when requesting certain non-audit services that may be allowed with safeguards, please be aware that this will not be a member of the audit team
• partners of an audit client, may not be appointed as a director of the audit client
• directors of the audit client, may not be contracted by the audit firm for any services, therefore if a new director is elected ensure this person is not in contract with the audit client
Auditor rotation

The Companies Act provides for the regular rotation of auditors. The designated auditor (not the firm) must be rotated every five years. The same individual (designated auditor) may not serve as the auditor or designated auditor of a company for more than five consecutive financial years. In terms of the transitional provisions set out in the Companies Act the five consecutive financial years contemplated in section 92 must be calculated from the date of commencement of this Act.

The effect of the transitional provision is that a designated auditor (the audit partner) only needs to rotate off a particular audit in five years’ time (or earlier, if required in terms of the IFAC rules, which requires rotation after seven years). This applies even if the audit partner had been the designated auditor of any number of years prior to the commencement of the new Act.

In terms of the provisions of the Act, an audit partner will be disqualified from serving as designated auditor as soon as he or she had served as designated auditor for more than five years. In effect, a partner that was appointed on 1 May 2011 may only serve until 1 May 2016.

Where an individual has served as the auditor or designated auditor of a company for two or more consecutive financial years and then ceases to be the auditor or designated auditor, the individual may not be appointed again as the auditor or designated auditor of that company until after the expiry of at least two further financial years (“cooling off period”).

The audit committee should take cognisance of developments internationally pertaining to mandatory audit firm rotation, and the prohibition of certain non-audit services. Although mandatory firm rotation is not effective in South Africa, the auditor of a group of companies may be affected where the holding company (in, for example Europe) is obliged to change audit firms, and decides to change the audit firm with respect to all its subsidiaries across the globe.

Quality of the audit

The audit committee can positively influence the quality of the audit through actively engaging with the auditor and questioning the auditor where there is concern that the audit quality is inappropriate. The motivation of the audit committee should not be on minimising cost since this may impact audit quality, but rather focusing on ensuring that sufficient, appropriate resources, including experts, have been involved on the audit and risks adequately addressed. The audit committee should consider evaluating audit quality and defining criteria for measuring the quality of the audit.
Evaluation of the independent auditor

Because there is no formal guidance regarding the evaluation of the independent auditor and because needs and preferences vary by company and audit committee, practices for evaluating the independent auditor range from highly formalised processes with extensive documentation to more informal processes. Factors the audit committee may consider in developing an evaluation process include:

- **Frequency and timing of the evaluation.** Many audit committees perform the evaluation annually, immediately following the fiscal-year financial reporting.

- **Parties involved in the assessment.** Although Section 94 of the Companies Act does not require the audit committee to evaluate the independent auditor, many conduct some form of evaluation to make decisions on auditor appointment and retention. As noted previously, Section 94 of the Act established the audit committee’s responsibility for the appointment, compensation, and oversight of the independent auditor. However, it may not be practical for the audit committee to oversee and coordinate the entire evaluation. In many instances, the audit committee delegates the coordination responsibility to the internal audit department or another group in the company.

- **Form and nature of the assessment.** Some independent auditors have assessment questionnaires for evaluating client service. Audit committees can use these questionnaires, tailor them to fit their needs, or create their own. The assessment can be done by having the relevant parties complete the questionnaire in writing or by holding interviews. They may also have a discussion about the experience the audit committee and others at the company have had in working with the independent auditors.
• Assessment criteria. The criteria for evaluating the independent auditor vary. Common criteria specific to the engagement team include technical competence, industry knowledge, frequency and quality of communication, cohesiveness as a team, and the level of support provided to the audit committee in fulfilling its responsibilities. Audit committees may consider information about the characteristics of the audit firm itself, such as size, financial strength and stability, presence in key markets, approach to professional development, technological capabilities, nature of the audit approach, quality of thought leadership, and eminence in the marketplace.
Section 5

Education and evaluation
Board education

With the enhanced focus on the responsibilities of boards and audit committees, continuing education for directors is an area of increasing importance. There are many options; for instance, public forums on corporate governance are offered by many professional services firms, universities, and not-for-profit organisations. Benefits include the opportunity to meet with peers and share experiences, and these programs can be invaluable for gaining knowledge from experts on trends in corporate governance. These forums often feature speakers who would not be available otherwise. However, boards should be careful not to rely completely on public programs designed for a broad audience, because they may not address the dynamics of a specific company and its industry.

An increasingly popular option is a customised program of continuing education focusing on topics such as roles and responsibilities, risk oversight, industry expertise, and financial literacy. Customised courses can address subjects relevant to the company’s needs and incorporate company-specific policies, processes, and objectives.

When designing a program of continuing education, the board should identify risks and complex issues facing the organisation. Directors can then evaluate their knowledge in these areas. This self-assessment can help the board gain a better picture of the issues it should include in the program. Depending on the organisation’s size and complexity, the board may want to enlist the internal auditors or outside consultants in the self-assessment process.

For the audit committee, the focus is more specific, centred on financial reporting and accounting issues such as revenue recognition, pensions and other post-employment benefits, financial instruments, critical accounting policies, and internal controls.

Once a curriculum is set, the board, the audit committee, and management should assess the resources available to create and deliver the program. The program should be developed using a mix of individuals—some with company knowledge and others with an external perspective.
In addition to continuing education, the company should consider orientation programs for new directors and audit committee members. Materials should include information on the company’s history and operations, corporate governance, industry trends, accounting policies and practices, company policies and the code of ethics, and major business and financial risks.

**Leading Practices**

- Provide orientation of new members with executives and independent auditors
- Consider offering continuing education programs in specialised or regulated industries, industry trends, reporting, operations, and related topics as well as particular issues relevant to the company and its business
- Offer one-on-one and committee-level education

Audit committees also benefit from periodically inviting subject-matter specialists to participate in audit committee meetings to enhance the committee’s knowledge and effectiveness. For example, specialists in international tax, governance, or a particular industry could provide valuable insight in addressing risks or new requirements. Independent auditors or outside consultants can assist in identifying appropriate specialists.
Audit committee performance evaluation

King III requires the board to perform an annual performance evaluation, and it recommends that this requirement be included in the audit committee’s charter. The Companies Act does not require audit committees to assess their performance, but the legislation itself may be the strongest argument for a robust evaluation process.

Performance assessment also provides information that the audit committee can use to improve processes. This is important because the independent auditor must consider the effectiveness of the audit committee’s oversight of financial reporting when evaluating the control environment. It is proposed that the following factors should be included in the consideration of the audit committee’s effectiveness:

- independence of the audit committee members from management
- clarity with which the audit committee’s responsibilities are articulated and the degree to which they are understood by management and the audit committee
- interaction of the audit committee and the independent auditor, the internal auditors, and senior financial executives
- whether the audit committee raises the right questions with management and the independent auditor, including questions that indicate its understanding of critical accounting policies and judgments
- whether the audit committee has been responsive to issues raised by the independent auditor.

Because there are no specific guidelines for assessing an audit committee’s performance, members and directors have the benefit and the burden of collaborating on an appropriate process. When advisable, this should be done in consultation with legal counsel.

There are several considerations in shaping the assessment process. First, there are various parties that may lead the assessment: the audit committee; the entire board or its nominating/governance committee; or the internal auditors. Some audit committees have found it useful to engage an objective third party to assist with the evaluation process. A combination of these may prove optimal. For example, a committee may choose to engage an adviser every two or three years, and facilitate the process internally in the other years.
The format of the evaluation is another consideration. In the case of a self-assessment, audit committee members may complete a questionnaire collectively or individually. If the internal auditors, the board, or management conducts the assessment, the format may consist of evaluation forms, interviews, or both. The party leading the evaluation may consider soliciting information from individuals who have significant interaction with the audit committee. The committee may want to consider changing the process periodically to keep it fresh.

Documentation is another significant concern, and the advice of corporate counsel is important in this matter. Regardless of the level of documentation in the evaluation process, the audit committee should identify and address opportunities for improvement.

Developing and executing a plan for improvement is the ultimate objective of the assessment. A performance evaluation may highlight the need to examine issues such as the audit committee’s composition and qualifications, information related to key financial reporting areas, members’ understanding of complex accounting and financial reporting issues, and meeting agendas.

A well-crafted performance assessment process can provide a number of benefits to the audit committee, including:

- prioritising the audit committee agendas and meeting structure to focus on the most critical issues
- shifting compliance oversight into the time between live meetings
- considering the committee’s composition in the context of current and future financial reporting challenges
- revisiting the timing, level of detail, and quality of materials provided by management
- identifying topics for continuing education

**Tools and resources.** See Annexure C for a sample audit committee performance evaluation.
Sample audit committee charter

Appendix A
Sample audit committee charter

This sample audit committee charter is based on a review of selected company charters, as well as the requirements of the Companies Act and the King Report on Governance for South Africa 2009 (King III). Deloitte does not accept any responsibility for any errors this publication may contain, whether caused by negligence or otherwise, or for any losses, however caused, sustained by any person that relies on it. The information presented can and will change; we are under no obligation to update such information. Deloitte makes no representations as to the sufficiency of these tools for your purposes, and, by providing them, we are not rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. These tools should not be viewed as a substitute for such professional advice or services, nor should they be used as a basis for any decision that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional adviser. Deloitte does not assume any obligations as a result of your access to or use of these tools.

This template is designed for SA public companies; exceptions to the requirements noted below may apply for certain companies, including investment companies, small-business issuers, and foreign private issuers. All companies should consult with legal counsel regarding the applicability and implementation of the various requirements identified.

Charter of the audit committee of the board of directors

1. Purpose

1.1. The audit and risk committee (the committee) is constituted as a statutory committee of [insert the name of the company] (the Company) in respect of the statutory duties in terms of section 94(7) of the Companies Act, 2008 and a committee of the board in all other duties assigned to it by the board.

1.2. Except with respect to the appointment, fees and terms of engagement of the independent auditor, the decisions of the committee do not reduce the individual and collective responsibilities of board members in regard to their fiduciary duties and responsibilities. Directors must ensure that they meet the standards of director’s conduct as provided for in section 76 of the Companies Act to act in good faith
and for a proper purpose, in the best interest of the company, and with the necessary care, skill and diligence.

1.3. This charter is subject to the provisions of the Companies Act and the company’s Memorandum of Incorporation, as well as and any other applicable law or regulatory provision.

1.4. The duties and responsibilities of the members of the committee as set out in this document are in addition to those duties and responsibilities that they have as members of the board.

1.5. The audit committee is appointed by the shareholders of the company for the primary purpose of assisting the board in:

1.5.1. Ensuring the continued independence of the independent auditor
1.5.2. Overseeing the external audit process
1.5.3. Overseeing integrated reporting
1.5.4. Applying the combined assurance model to ensure a coordinated approach to all assurance activities
1.5.5. Reviewing, the expertise, resources and experience of the finance function
1.5.6. Considering the appropriateness of the expertise and experience of the financial director
1.5.7. Overseeing the internal audit function
1.5.8. Oversight of internal controls and financial reporting
1.5.9. Risk assessment and oversight

1.6. Consistent with these functions, the audit committee should encourage continuous improvement of, and should foster adherence to, the company’s policies, procedures, and practices at all levels. The audit committee should also provide for open communication among the independent auditor, financial and senior management, the internal audit function, and the board of directors.

2. Membership

2.1 The committee shall be appointed annually by the shareholders and shall comprise at least three members.

2.2 The board, through the nominations committee, shall identify and nominate suitably skilled and experienced directors for appointment by the shareholders.

2.3 The board shall fill a vacancy on the committee within 40 business days, to be ratified by shareholders at the next annual general meeting.

2.4 The audit committee must consist of at least three members. Each member of the committee must be a director of the company and not:
2.4.1 be involved in the day to day management of the company for the past financial year
2.4.2 be a full-time employee of the company for the past 3 financial years
2.4.3 be a material supplier or customer of the company such that a reasonable and informed third party would conclude in the circumstances that the integrity, impartiality or objectivity of that director is compromised by that relationship, and
2.4.4 be related to anybody who falls within the above criteria.
2.5 All members of the committee shall have general financial knowledge, at least one of whom shall have recent and relevant financial experience. Collectively, the committee should have an understanding of all matters that are integral to the company’s integrated report.
2.6 The board shall appoint the chairman of the committee. In the absence of the chairman of the committee and/or an appointed deputy, the remaining members present shall elect one of themselves to chair the meeting.
2.7 Only members of the committee shall have the right to vote. However, other individuals such as the Chairman of the board, the Chief Executive Officer, the Chief Financial Officer, the Head of Internal Audit and other representatives from the finance department may be invited to attend for all or part of any meeting as and when considered appropriate by the committee.
2.8 The independent auditors shall be invited to attend meetings of the committee on a regular basis.

3. Secretary
3.1 The company secretary of the company, or its nominee, shall act as the secretary of the committee.

4. Quorum
4.1 The quorum necessary for the transaction of business shall be constituted by a majority of the members of the committee. A duly convened meeting of the committee at which a quorum is present shall be competent to exercise all or any of the authorities, powers and discretions vested in or exercisable by the committee.
5. Frequency of Meetings

5.1 The committee shall meet at least four times a year at appropriate times in the reporting and audit cycle and additionally as the chairman of the committee considers necessary. The external or internal auditors may request a meeting, if they consider one is necessary, as may any committee member.

6. Notice of Meetings and Agenda

6.1 Meetings of the committee shall be convened by the secretary of the committee at the request of the chairman of the committee.

6.2 Unless otherwise agreed, notice of each meeting confirming the venue, time and date, together with an agenda of items to be discussed, shall be forwarded to each member of the committee, and any other person required to attend, no later than one week prior to the meeting. Supporting papers shall be sent to committee members, and to other attendees as appropriate, at the same time.

6.3 The chairman will approve the agenda for committee meetings and any member may suggest items for consideration.

7. Minutes of Meetings

7.1 The secretary shall minute the proceedings and resolutions of all meetings of the committee, including the names of those present and in attendance.

7.2 The secretary shall ascertain, at the beginning of each meeting, the existence of any conflicts of interest and minute them accordingly. If any conflict of interest exists, the director subject to the conflict shall not participate or vote on the issue giving rise to the conflict.

7.3 Minutes of committee meetings shall be circulated promptly to all members of the committee and, once agreed, to all members of the board, unless a conflict of interest exists, and to the independent auditors and the CAE.

7.4 The minutes of the committee shall be formally approved at its next scheduled meeting.

8. Annual General Meeting

8.1 The chairman of the committee shall attend the Annual General Meetings of the company and be prepared to respond to any shareholder questions on the committee’s activities.
9. Duties

9.1 Independent (External) Audit

_The committee shall:_

9.1.1 consider and make recommendations to the board, to be put to shareholders for approval at the Annual General Meetings of the company, in relation to the appointment, re-appointment and removal of the company’s independent auditors. The committee shall oversee the selection process for new auditors and if an auditor resigns the committee shall investigate the issues leading to this and decide whether any action is required;

9.1.2 ensure that the appointment of the auditor complies with the Companies Act, the Auditing Profession Act and other relevant legislation;

9.1.3 oversee the relationship with the independent auditors including (but not limited to):

9.1.3.1 determining their remuneration, whether fees for audit or non-audit services;

9.1.3.2 approving their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;

9.1.3.3 assessing their independence and objectivity annually taking into account relevant professional and regulatory requirements and the relationship with the auditor as a whole, including the provision of any non-audit services;

9.1.3.4 satisfying itself that there are no relationships (such as family, employment, investment, financial or business) between the auditors and the company (other than in the ordinary course of business);

9.1.3.5 agreeing with the board a policy on the employment of former employees of the company’s auditors, then monitoring the implementation of this policy;

9.1.3.6 monitoring the auditors’ compliance with relevant ethical and professional guidance on the rotation of audit partners, the level of fees paid by the company compared to the overall fee income of the firm, office and partner and other related requirements;

9.1.3.7 assessing annually their qualifications, expertise and resources and the effectiveness of the audit process which shall include a report from the independent auditors on their own internal quality procedures;

9.1.3.8 considering the risk of the withdrawal of the company’s auditors from the market; and
9.1.3.9 at least annually, obtaining and reviewing a report by the independent auditor describing:
9.1.3.9.1 the independent auditor’s internal quality-control procedures;
9.1.3.9.2 any material issues raised by the most recent internal quality-control review or peer review, or by any inquiry or investigation conducted by governmental or professional authorities during the preceding five years with respect to independent audits carried out by the independent auditor, and any steps taken to deal with such issues
9.1.3.9.3 all relationships between the independent auditor and the company
9.1.4 meet regularly with the independent auditors, including once at the planning stage before the audit and once after the audit at the reporting stage. The committee shall meet the independent auditors at least once a year, without management being present, to discuss their remit and any issues arising from the audit;
9.1.5 review and approve the annual audit plan and ensure that it is consistent with the scope of the audit engagement;
9.1.6 review the findings of the audit with the independent auditors. This shall include but not be limited to, the following:
9.1.6.1 a discussion of any major issues which arose during the audit;
9.1.6.2 a discussion and review of any problems or difficulties with management’s response to audit issues, and oversee any disagreements between management and the auditors if they arise;
9.1.6.3 any accounting and audit judgements; and
9.1.6.4 levels of errors identified during the audit.
9.1.7 review the effectiveness of the audit process annually;
9.1.8 review any representation letter(s) requested by the independent auditors before they are signed by management;
9.1.9 review the management letter and management’s response to the auditors’ findings and recommendations;
9.1.10 distinguish between audit and non-audit services, and develop and implement a policy on the supply of non-audit services by the independent auditors, taking into account any relevant ethical guidance on the matter;
9.1.11 pre-approve the contracts for
non-audit services to be rendered by
the independent auditor and consider
whether the auditor’s provision of
non-audit services is compatible with the
auditor’s independence; and
9.1.12 recommend to the board to engage an
external assurance provider to provide
assurance over material elements (such
elements should be determined by the
relevant committee responsible for
overseeing the sustainability reporting)
of the sustainability part of the
integrated report. The audit committee
should evaluate the independence and
credentials of this external assurance
provider.

9.2 Financial Reporting

The committee shall:
9.2.1 monitor the integrity of the financial
statements of the company, including
its annual and half-yearly reports,
preliminary results announcements and
any other formal announcement relating
to its financial performance, reviewing
significant financial reporting issues and
judgements which they contain; and
9.2.2 review summary financial statements,
significant financial returns to regulators
and any financial information contained
in certain other documents, such as
announcements of a price sensitive
nature, provided that such monitoring
and review is not inconsistent with
any requirement for prompt reporting
under the listing requirements of the
Johannesburg Stock Exchange;
9.2.3 ensure that a combined assurance model
is applied to provide a coordinated
approach to all assurance activities, and in
particular:
9.2.3.1 ensure that the combined assurance
received is appropriate to address all the
significant risks facing the company; and
9.2.3.2 monitor the relationship between the
external assurance providers and the
company;
9.2.4 understand the scope of the internal
and independent auditors’ review of
internal control over financial reporting
and obtain reports on significant findings
and recommendations, together with
management responses;
9.2.5 receive and review any disclosure from
the company’s CEO or CFO made in
connection with the certification of the
company’s quarterly and annual reports of:
9.2.5.1 significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company’s ability to record, process, summarise, and report financial data; and

9.2.5.2 any fraud, whether or not material, that involves management or other employees who have a significant role in the company’s internal controls;

9.2.6 review major issues regarding accounting principles and financial statement presentations, including any significant changes in the company’s selection or application of accounting principles; major issues as to the adequacy of the company’s internal controls; and any special audit steps adopted in light of material control deficiencies;

9.2.7 review analyses prepared by management and/or the independent auditor setting forth significant financial reporting issues and judgments made in connection with the preparation of the financial statements;

9.2.8 review the effect of regulatory and accounting initiatives, as well as off-balance-sheet structures, on the financial statements of the company; and

9.2.9 assist the board in reviewing the integrated report to ensure that the information is reliable and that it does not contradict the financial aspects of the report.

The committee shall review and challenge where necessary:

9.2.10 the consistency of, and any changes to, accounting policies both on a year on year basis and across the company;

9.2.11 the methods used to account for significant or unusual transactions where different approaches are possible;

9.2.12 whether the company has followed appropriate accounting standards and made appropriate estimates and judgements, taking into account the views of the independent auditors;

9.2.13 the clarity of disclosure in the company’s financial reports and the context in which statements are made; and

9.2.14 all material information presented with the financial statements, such as the operating and financial review, the corporate governance statement (insofar as it relates to the audit and risk management) and the disclosure on sustainability issues (to ensure no conflict with financial information).
9.3 Whistle blowing and fraud

The committee shall:

9.3.1 review the company’s arrangements for its employees to raise concerns, in confidence, about possible wrongdoing in financial reporting or other matters. The committee shall ensure that these arrangements allow proportionate and independent investigation of such matters and appropriate follow up action;

9.3.2 ensure that there is a process in place to be informed of any reportable irregularities (as identified in the Auditing Profession Act, 2005) identified and reported by the independent auditor; and

9.3.3 review the company’s procedures for detecting and preventing fraud and bribery and receiving reports on non-compliance.

9.4 Internal Audit

The committee shall:

9.4.1 monitor and review the effectiveness of the company’s internal audit function in the context of the company’s overall internal controls and risk management systems, including giving consideration to periodic independent quality review of the function as deemed appropriate;

9.4.2 approve the appointment and removal of the CAE;

9.4.3 consider and approve the remit of the internal audit function and ensure it has adequate resources, skills, qualifications and appropriate access to information to enable it to perform its function effectively and in accordance with the relevant professional standards. The committee shall also ensure the function has adequate standing and is free from management or other restrictions;

9.4.4 approve the internal audit charter and perform an annual review of the charter, making recommendations for changes if required;

9.4.5 review and approve the annual internal audit plan;

9.4.6 evaluate the formal review of financial controls conducted annually by the internal audit function on behalf of the board and report to the board and shareholders on the effectiveness of the company’s internal controls;

9.4.7 review all reports on the company from the CAE, including managements responsiveness to findings and recommendations;
9.4.8 meet the CAE at least once a year, without management being present, to discuss their remit and any issues arising from the internal audits carried out. In addition, the CAE shall have the right of direct access to the chairman of the board and to the committee; and

9.4.9 perform an annual assessment of the internal audit function’s responsibility, budget and staffing, with input from the independent auditor.

9.5 Reporting Responsibilities

9.5.1 The chairman of the committee shall report formally to the board on its proceedings after each meeting on all matters within its duties and responsibilities.

9.5.2 The committee shall make whatever recommendations to the board it deems appropriate on any area within its remit where action or improvement is needed.

9.5.3 The committee shall consider, on an annual basis, and satisfy itself of the appropriateness of the expertise of the chief financial officer (acting as the financial director) and will report to shareholders in the company’s Annual Report that it has executed this responsibility.

9.5.4 The committee shall compile a report to shareholders on its activities to be included in the company’s annual financial statements:

9.5.4.1 describing how the audit committee carried out its functions

9.5.4.2 stating whether the audit committee is satisfied that the auditor was independent of the company, and

9.5.4.3 commenting in any way the committee considers appropriate on the financial statements, the accounting practices and the internal financial control of the company.

9.6 Other Matters

*The committee shall:*

9.6.1 have access to sufficient resources in order to carry out its duties, including access to the Company secretary of the company for assistance as required;

9.6.2 be provided with appropriate and timely training, both in the form of an induction programme for new members and on an on-going basis for all members;

9.6.3 at least once a year, review the appropriateness of the expertise, experience and adequacy of resources of the company finance function;
9.6.4 oversee any investigation of activities which are within its terms of reference and act as a court of the last resort; and

9.6.5 at least once a year, review its own performance, constitution and terms of reference to ensure it is operating at maximum effectiveness and recommend any changes it considers necessary to the board for approval.

10. Authority

The committee derives its authority from the statutory duties as contained in section 94 of the Companies Act, as well as from the delegated authority of the board as contained in this document. The committee is authorised:

10.1 to conduct investigations into any matters within its scope of responsibility;

10.2 to seek any information it requires from any employee, officer or director of any company in the company or external party in order to perform its duties;

10.3 to obtain, at the company’s expense, any outside legal or other professional advice it shall reasonably require in connection with the performance of its duties;

10.4 to require the chairmen of the other board committees, any of the executive directors, any officer of the company, company secretary or assurance providers to provide it with information;

10.5 to call any employee to be questioned at a meeting of the committee as and when required;

10.6 to have the right to publish in the company’s integrated report details of any issues that cannot be resolved between the committee and the board; and

10.7 to form, and delegate authority to, subcommittees and may delegate authority to one or more designated members of the committee.

The committee has decision-making authority in regard to its statutory duties of verifying the independence of the independent auditor, determining the fee for the independent auditor, and for the terms of engagement of the independent auditor.
Audit committee planning tool

Appendix B
Audit committee calendar of activities

Audit committees can use this tool to help plan their annual activities and meeting agendas. It considers the requirements for the audit committees as per the Companies Act, 2008, King III and the JSE Listings Requirements, as well as common practices in the marketplace and is subject to change if additional guidance is issued. The “Results From:” section indicates if the action or responsibility results from a requirement of the Companies Act, 2008, King III and the JSE Listings Requirements, or a common or emerging practice. The action or responsibility, as described, may not be an explicit legislative or regulatory requirement or proposal, but may be an action that logically results from other legislative or regulatory requirements or proposals. The “Suggested Frequency” section offers a benchmark for how often the activity should be performed, while the “Meeting Month” section provides an area where the audit committee can mark the months in which an activity should be performed. The audit committee should use this tool in conjunction with the “Sample Audit Committee Charter,” and it should be tailored to reflect the responsibilities in the company’s audit committee charter.

This document is not an all-inclusive list of activities that an audit committee should or must execute. The planning tool contains general information only and does not constitute, and should not be regarded as, legal or similar professional advice or service. Deloitte does not accept any responsibility for any errors this publication may contain, whether caused by negligence or otherwise, or for any losses, however caused, sustained by any person that relies on it. The information presented can and will change; we are under no obligation to update such information. Deloitte makes no representations as to the sufficiency of these tools for your purposes, and, by providing them, we are not rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. These tools should not be viewed as a substitute for such professional advice or services, nor should they be used as a basis for any decision that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional adviser. Deloitte does not assume any obligations as a result of your access to or use of these tools.

This planning tool is designed for South African companies. All companies should consult with legal counsel regarding the applicability and implementation of the various activities identified.
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<th>Action/Responsibility</th>
<th>Companies Act 2008</th>
<th>King III</th>
<th>JSE Listings Requirements</th>
<th>Other Requirement</th>
<th>Common Practice</th>
<th>Suggested Frequency</th>
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<td>General Responsibilities</td>
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<td>Review audit committee members’ compliance with applicable independence rules and</td>
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<td>As necessary, engage outside legal, accounting, or other advisers and provide funding</td>
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<td>Report regularly to the board of directors regarding the execution of duties and</td>
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<td>Review the financial literacy and expertise of all audit committee members. Determine</td>
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<td>audit committee financial expert status and determine that members are in compliance</td>
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<td>Conclude each regular audit committee meeting with an executive session of the</td>
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<td>Periodically, meet with management privately to discuss any necessary matters.</td>
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<td><strong>Consider and plan for succession of audit committee members</strong></td>
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<td><strong>Review, with management, the company’s finance function, including its budget, organisation and quality of personnel</strong></td>
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<td><strong>Review of Financial/Controls Information</strong></td>
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<td>Review and discuss with management and the independent auditors the company’s annual financial statements prior to filing.</td>
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<td>Review the internal auditor’s assessment of internal controls.</td>
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<td>Review other reports rendered by the independent auditors and submitted by the company to any governmental body or the public.</td>
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<td>Discuss the financial information and earnings guidance provided to analysts and ratings agencies. This discussion may be in general terms.</td>
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<td>Review the regular internal reports to management prepared by the internal audit</td>
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<td>Nnominate an independent auditor for appointment by the shareholders.</td>
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<td>Compensate, retain, and oversee the work of the independent auditor for the purpose</td>
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<td>Review the performance of the independent auditor, including the lead audit partner.</td>
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<td>Ensure that partners are rotated in accordance with applicable requirements.</td>
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<td>Pre-approve audit and non-audit services provided by the independent auditor.</td>
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1. **Consider the independence of the auditor**, including engaging in dialogue with the independent auditor with respect to any disclosed relationships or services that may affect the independence and objectivity of the auditor and take appropriate actions to oversee independence.

   - **Companies Act 2008**: Annually and as needed
   - **King III**: Annually and as needed
   - **JSE Listings Requirements**: Annually and as needed
   - **Other Requirement**: Annually and as needed
   - **Common Practice**: Annually and as needed

2. **Oversee the resolution of disagreements between management and the independent auditor if they arise.**

   - **Companies Act 2008**: Annually and as needed
   - **King III**: Annually and as needed
   - **JSE Listings Requirements**: Annually and as needed
   - **Other Requirement**: Annually and as needed
   - **Common Practice**: Annually and as needed

3. **Review with the independent auditor any problems or difficulties encountered in the course of the audit and management’s response.**

   - **Companies Act 2008**: Annually and as needed
   - **King III**: Annually and as needed
   - **JSE Listings Requirements**: Annually and as needed
   - **Other Requirement**: Annually and as needed
   - **Common Practice**: Annually and as needed

4. **Review the audit plan and scope with the independent auditor.**

   - **Companies Act 2008**: Annually and as needed
   - **King III**: Annually and as needed
   - **JSE Listings Requirements**: Annually and as needed
   - **Other Requirement**: Annually and as needed
   - **Common Practice**: Annually and as needed

5. **Review written communications between the independent auditor and management, including (but not limited to) the management letter and schedule of unadjusted differences.**

   - **Companies Act 2008**: As reported by the independent auditor
   - **King III**: As reported by the independent auditor
   - **JSE Listings Requirements**: As reported by the independent auditor
   - **Other Requirement**: As reported by the independent auditor
   - **Common Practice**: As reported by the independent auditor
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<th>Action/Responsibility</th>
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<td>Periodically, meet with the independent auditor privately to discuss any matters necessary.</td>
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<td><strong>Financial Reporting Processes, Accounting Policies, and Internal Control</strong></td>
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<td>In consultation with the independent auditor and the internal audit function, review the integrity of the company’s financial reporting processes (both internal and external) and the internal control structure (including disclosure controls and procedures and internal control over financial reporting).</td>
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<td>In consultation with the independent auditor and the internal audit function and management, review the combined assurance model.</td>
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<tr>
<td>Action/Responsibility</td>
<td>Companies Act 2008</td>
<td>King III</td>
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<tr>
<td>Review with management major issues regarding accounting principles and presentation of the financial statements, including any significant changes in the company’s selection or application of accounting principles, major issues as to the adequacy of the company’s internal controls, and any special audit steps adopted in response to material control deficiencies.</td>
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<tr>
<td>Review management’s analyses of financial reporting issues and judgments made in connection with the preparation of the financial statements.</td>
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<tr>
<td>Review with management the effect of regulatory and accounting initiatives, as well as off-balance-sheet structures, on the financial statements of the company.</td>
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<tr>
<td>Review and approve all related-party transactions.</td>
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<tr>
<td>Action/Responsibility</td>
<td>Results From:</td>
<td>Meeting Month</td>
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<td></td>
<td>Companies Act 2008</td>
<td>January</td>
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<tr>
<td>Review the adequacy of procedures for the receipt, retention, and treatment of complaints regarding accounting, internal control, or auditing matters, including procedures for confidential, anonymous submissions by company employees.</td>
<td>King III</td>
<td>Semiannually or quarterly</td>
</tr>
<tr>
<td>Receive and review reports or complaints of questionable accounting, auditing, or internal control matters.</td>
<td>JSE Listings Requirements</td>
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<td></td>
<td>Other Requirement</td>
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<td>Common Practice</td>
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</table>

**Internal Audit Activities**

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<tr>
<th>Action/Responsibility</th>
<th>Results From:</th>
<th>Meeting Month</th>
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<tbody>
<tr>
<td></td>
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<td>January</td>
</tr>
<tr>
<td>Review and advise on the selection or removal of the Chief Audit Executive.</td>
<td>King III</td>
<td>As needed</td>
</tr>
<tr>
<td>Periodically, meet with Internal Audit privately to discuss any necessary matters.</td>
<td>King III</td>
<td>Quarterly</td>
</tr>
<tr>
<td>Periodically, review with Internal Audit any significant difficulties, disagreements with management, or scope restrictions encountered in the course of the function’s work.</td>
<td>King III</td>
<td>Annually</td>
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<tr>
<td>Action/Responsibility</td>
<td>Results From:</td>
<td>Meeting Month</td>
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<tr>
<td>Review the activities and organisational structure of the internal audit function,</td>
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<td>as well as the qualifications of its personnel.</td>
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<td>Review the internal audit charter and plan and recommend any necessary changes.</td>
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<tr>
<td>Periodically review, with Internal Audit, the internal audit function’s responsibilities, budget, and staffing.</td>
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<tr>
<td><strong>Risk Management</strong></td>
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<tr>
<td>Discuss with management significant risk exposures, including major financial and</td>
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<tr>
<td>accounting risk exposures, and the steps taken by management to control them.</td>
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</tbody>
</table>

**Common Practice**

- Annually
<table>
<thead>
<tr>
<th>Action/Responsibility</th>
<th>Companies Act 2008</th>
<th>King III</th>
<th>JSE Listings Requirements</th>
<th>Other Requirement</th>
<th>Common Practice</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prepare a report, to be included in the annual financial statements for that financial year</td>
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<tr>
<td>1. describing how the audit committee carried out its functions</td>
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<tr>
<td>2. stating whether the audit committee is satisfied that the auditor was independent of the company, and</td>
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<tr>
<td>3. commenting in any way the committee considers appropriate on the financial statements, the accounting practices and the internal financial control of the company</td>
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<tr>
<td>Action/Responsibility</td>
<td>Companies Act 2008</td>
<td>King III</td>
<td>JSE Listings Requirements</td>
<td>Other Requirement</td>
<td>Common Practice</td>
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<td>Oversee the integrated reporting process:</td>
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<td>1. Consider all factors and risks that may impact on the integrity of the</td>
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<tr>
<td>integrated report</td>
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<td>2. Review the annual financial statements</td>
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<td>3. Comment in the annual financial statements on the financial statements, the</td>
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<td>accounting practices and the effectiveness of the internal financial controls</td>
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<td>4. Review the disclosure of sustainability issues in the integrated report to</td>
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<td>ensure that it is reliable and does not conflict with the financial information</td>
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<td>5. Recommend to the board whether or not to engage an external assurance provider</td>
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<td>on material sustainability issues</td>
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<td>6. Recommend the integrated report for approval by the board</td>
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<tr>
<td>Action/Responsibility</td>
<td>Results From:</td>
<td>Suggested Frequency</td>
<td>Meeting Month</td>
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<tr>
<td>Review the audit committee charter; recommend to the board of directors any necessary amendments, as conditions dictate.</td>
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<td>Annually</td>
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<tr>
<td>Review, with the independent auditors, the internal audit function, and management, the extent to which changes or improvements in financial or accounting practices, as approved by the audit committee, have been implemented.</td>
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<td>Annually</td>
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<tr>
<td>Participate in appropriate continuing education.</td>
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<td>As needed</td>
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<tr>
<td>Assess performance relative to the audit committee’s purpose, duties, and responsibilities.</td>
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<td>Annually</td>
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</table>
Audit committee performance evaluation

Appendix C
Audit committee performance evaluation

The following questionnaire is based on emerging and leading practices to assist in the self-assessment of an audit committee’s performance. It is not intended to be all-inclusive.

When completing the performance evaluation, consider the following process:

• Select a coordinator and establish a timeline for the process.
• In addition to audit committee members completing the form as a self-evaluation, ask individuals who interact with the audit committee members to provide feedback.
• Ask each audit committee member to complete an evaluation by selecting the appropriate rating that most closely reflects the audit committee’s performance related to each practice.
• Consolidate into a summarised document for discussion and review by the committee.

For each of the following statements, select a number between 1 and 5, with 1 indicating that you strongly disagree and 5 indicating that you strongly agree with the statement. Select 0 if the point is not applicable or you do not have enough knowledge or information to rank the organisation’s audit committee on a particular statement.
## Rank each of these statements

<table>
<thead>
<tr>
<th>Composition and Quality</th>
<th>- Not applicable</th>
<th>Strongly disagree</th>
<th>2 - Disagree</th>
<th>3 - Acceptable</th>
<th>4 - Agree</th>
<th>5 - Strongly agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Qualified audit committee members are identified by sources independent of management (e.g., independent board members assisted by an outside search firm).</td>
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<tr>
<td>2. Audit committee members have the appropriate qualifications to meet the objectives of the audit committee’s charter, including appropriate financial literacy.</td>
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<td>3. The audit committee demonstrates integrity, credibility, trustworthiness, active participation, an ability to handle conflict constructively, strong interpersonal skills, and the willingness to address issues proactively.</td>
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<td>4. The audit committee demonstrates appropriate industry knowledge and includes a diversity of experiences and backgrounds.</td>
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<td>5. Members of the audit committee meet all applicable independence requirements.</td>
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<tr>
<td>6. The audit committee participates in a continuing education program to enhance its members’ understanding of relevant accounting, reporting, regulatory, auditing, and industry issues.</td>
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<tr>
<td>7. The audit committee monitors compliance with the Companies Act, King III and other relevant corporate governance regulations and guidelines.</td>
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<td>8. The audit committee reviews its charter annually to determine whether its responsibilities are described adequately and recommends changes to the board for approval.</td>
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<td>9. New audit committee members participate in an orientation program to educate them on the company, their responsibilities, and the company’s financial reporting and accounting practices.</td>
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<td>10. The audit committee chairman is an effective leader.</td>
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<td>11. The audit committee, in conjunction with the nominations committee (or its equivalent), creates a succession and rotation plan for audit committee members, including the audit committee chairman.</td>
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<tr>
<td>Rank each of these statement</td>
<td>- Not applicable</td>
<td>Strongly disagree</td>
<td>2 - Disagree</td>
<td>3 - Acceptable</td>
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<td>5 - Strongly agree</td>
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<td><strong>Composition and Quality</strong></td>
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<tr>
<td><strong>Understanding the Business, including Risks</strong></td>
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<td>12. The audit committee considers or knows that the full board or other committees take into account significant risks that may directly or indirectly affect financial statement reporting. Examples include:</td>
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<td>• Regulatory and legal requirements</td>
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<td>• Concentrations (e.g., suppliers and customers)</td>
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<td>• Market and competitive trends</td>
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<td>• Financing and liquidity needs</td>
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<tr>
<td>• Financial exposures</td>
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<tr>
<td>• Business continuity</td>
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<td>• Company reputation</td>
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<td>• Financial strategy execution</td>
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<td>• Financial management’s capabilities</td>
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<td>• Management override</td>
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<td>• Fraud control</td>
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<td>• Company pressures, including “tone at the top”</td>
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<td>13. The audit committee considers, understands, and approves the process implemented by management to effectively identify, assess, and respond to the organisation’s key risks.</td>
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<td>14. The audit committee understands and approves management’s fraud risk assessment and has an understanding of identified fraud risks.</td>
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<td>15. The audit committee considers the company’s performance versus that of its peers in a manner that enhances comprehensive risk oversight by using reports provided directly by management to the audit committee or at the full board meeting. These may include benchmarking information comparing the company’s financial performance and ratios with industry competitors and peers, industry trends, analyst estimates, and budget analysis with explanations for areas where significant differences are apparent.</td>
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</table>
### Composition and Quality

<table>
<thead>
<tr>
<th>Process and Procedures</th>
<th>1 - Not applicable</th>
<th>2 - Disagree</th>
<th>3 - Acceptable</th>
<th>4 - Agree</th>
<th>5 - Strongly agree</th>
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<tbody>
<tr>
<td>16. The audit committee reports its proceedings and recommendations to the board after each committee meeting.</td>
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<td>17. The audit committee develops a calendar that dedicates the appropriate time and resources needed to execute its responsibilities.</td>
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<td>18. Audit committee meetings are conducted effectively, with sufficient time spent on significant or emerging issues.</td>
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<td>19. The level of communication between the audit committee and relevant parties is appropriate; the audit committee chairman encourages input on meeting agendas from committee and board members, management, the internal auditors, and the independent auditors.</td>
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<td>20. The audit committee sets clear expectations and provides feedback to the full board concerning the competency of the organisation’s CFO and senior financial management.</td>
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<td>21. The audit committee has input into the succession planning process for the CFO.</td>
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<td>22. The agenda and related information (e.g., prior meeting minutes, press releases, and financial statements) are circulated in advance of meetings to allow audit committee members sufficient time to study and understand the information.</td>
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<td>23. Written materials provided to audit committee members are relevant and concise.</td>
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<td>24. Meetings are held with enough frequency to fulfill the audit committee’s duties and at least quarterly, which should include periodic visits to company locations with key members of management.</td>
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<td>25. Regularly, audit committee meetings include separate private sessions with financial management and the internal and independent auditors.</td>
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<td>26. The audit committee maintains adequate minutes of each meeting.</td>
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<td>27. The audit committee and the remuneration committee regularly review management incentive plans to consider whether the incentive process is appropriate.</td>
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<tr>
<td>Rank each of these statement</td>
<td>- Not applicable</td>
<td>2 - Disagree</td>
<td>3 - Acceptable</td>
<td>4 - Agree</td>
<td>5 - Strongly agree</td>
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<tr>
<td>Composition and Quality</td>
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<td>28. The audit committee meets periodically with the committee responsible for reviewing the company’s disclosure procedures.</td>
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<td>29. The audit committee respects the line between oversight and management of the financial reporting process.</td>
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<td>30. Audit committee members come to meetings well prepared.</td>
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<tr>
<td>Oversight of the Financial Reporting Process, including Internal Controls</td>
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<td>31. The audit committee considers the quality and appropriateness of financial accounting and reporting, including the transparency of disclosures.</td>
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<tr>
<td>32. The audit committee reviews the company’s significant accounting policies.</td>
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<td>33. The audit committee understands and approves the process used by management to identify and disclose related-party transactions.</td>
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<td>34. The audit committee oversees the organisation’s external financial reporting and internal control over financial reporting.</td>
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<td>35. The audit committee receives sufficient information to assess and understand management’s process for evaluating the organisation’s system of internal controls (e.g., financial reporting and disclosure controls, operation controls, compliance controls) and also believes that management’s scope of internal control testing adequately supports its internal control assessment.</td>
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<td>36. The audit committee understands and gives appropriate consideration to the internal control testing conducted by management, the internal auditors, and the independent auditors to assess the process for detecting internal control issues or fraud (combined assurance model). Any significant deficiencies or material weaknesses that are identified are addressed, reviewed, and monitored by the audit committee.</td>
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<td>37. The audit committee makes inquiries of the independent auditors, internal auditors, and management on the depth of experience and sufficiency of the company’s accounting and finance staff.</td>
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<tr>
<td>Rank each of these statement</td>
<td>- Not applicable</td>
<td>Strongly disagree</td>
<td>2 - Disagree</td>
<td>3 - Acceptable</td>
<td>4 - Agree</td>
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<td><strong>Composition and Quality</strong></td>
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<td>38. The audit committee reviews the management recommendation letters written by the independent and internal auditors and monitors the process to determine that all significant matters are addressed.</td>
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<td><strong>Circle one number for each statement</strong></td>
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<td>39. The audit committee oversees that management takes action to achieve resolution when there are repeat comments from auditors, particularly those related to internal controls.</td>
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<td>40. Adjustments to the financial statements that resulted from the audit are reviewed by the audit committee, regardless of whether they were recorded by management.</td>
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<td>41. The audit committee is consulted when management is seeking a second opinion on an accounting or auditing matter.</td>
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<td><strong>Oversight of Audit Functions</strong></td>
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<td>42. The audit committee understands the coordination of work between the independent and internal auditors and clearly articulates its expectations of each.</td>
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<td>43. The audit committee regularly reviews the adequacy of the internal audit function (e.g., the charter; audit plan; budget; compliance; and number, quality, and continuity of staff).</td>
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<td>44. The audit committee oversees the role of the internal audit director from selection to termination (e.g., appointment, evaluation, compensation, and retention) and provides feedback at least annually.</td>
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<td>45. The internal audit reporting lines established with the audit committee promote an atmosphere where significant issues that might involve management will be brought to the attention of the audit committee.</td>
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<td>46. The audit committee appropriately considers internal audit reports, management’s responses, and steps toward improvement.</td>
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<td>47. The audit committee oversees the role of the independent auditors from selection to termination and has an effective process to evaluate the independent auditors’ qualifications and performance.</td>
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<td>Composition and Quality</td>
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<td>48. The audit committee considers the independent audit plan and provides recommendations.</td>
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<td>49. The audit committee determines the audit fees paid to the independent auditors</td>
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<td>50. The audit committee comprehensively reviews management’s representation letters to the independent auditors, including making inquiries about any difficulties in obtaining the representations.</td>
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<td>51. The audit committee pre-approves all audit and non-audit services provided by the independent auditors and considers the scope of the non-audit services provided.</td>
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<td>52. The audit committee reviews other professional services that relate to financial reporting (e.g., consulting, legal, and tax strategy services) provided by outside consultants.</td>
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<td>53. The audit committee monitors the process to determine that the independent auditors’ partners are rotated in accordance with applicable rules.</td>
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<td>54. The audit committee has private executive sessions with management and the internal and independent auditors that result in candid discussion of pertinent issues.</td>
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<tr>
<th>Monitoring Activities</th>
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<tr>
<td>55. An annual performance evaluation of the audit committee is conducted and any matters that require follow-up are resolved and presented to the full board.</td>
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<td>56. The company provides the audit committee with sufficient funding to fulfill its objectives and engage external parties for matters requiring external expertise.</td>
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</table>
Public sector perspective

Appendix D
Public sector perspective

In terms of the Public Finance Management Act (PFMA) and related Treasury regulations applicable to Public Entities [Sections 51(1)(a)(ii) and 76(4)(d) of the PFMA], the board of directors (known as the Accounting Authority in terms of the PFMA) of such Public Entities must establish an audit committee as a subcommittee of the accounting authority. A shared audit committee may be established for a public entity and any subsidiaries under the ownership and control of that entity.

The following are specific requirements in relation to the constitution and activities of an Audit Committee of a Public Entity:

- the chairperson of the audit committee must be independent, be knowledgeable of the status of the position, have the requisite business, financial and leadership skills and may not be the chairperson of the accounting authority or a person who fulfils an executive function in the public entity
- the majority of the members of an audit committee of a Public Entity shall consist of non-executive members appointed by the accounting authority, although committee members need not all be members of the accounting authority. The majority of persons serving on an audit committee must be financially literate
- the relevant portfolio Minister under which the Public Entity resorts (known as the Executive Authority) must concur with any premature termination of services of a member of the audit committee
- the audit committee must operate in terms of written terms of reference, which must deal adequately with its membership, authority and responsibilities. The terms of reference must be reviewed at least annually to ensure its relevance. It must further be disclosed in the entity’s integrated report whether or not the audit committee has adopted a formal terms of reference and if so, whether the committee satisfied its responsibilities for the year, in compliance with its terms of reference. The audit committee of a Public Entity has explicit authority to investigate matters within its powers, as identified in the written terms of reference
- the audit committee must be provided with the resources it needs to investigate such matters and shall have full access to information. The audit committee must safeguard all information supplied to it within the ambit of the law
- should a report from internal audit (or any other source) to the audit committee implicate any member(s) of the accounting authority in fraud, corruption or gross negligence, the chairperson of the audit committee must promptly report this to the relevant executive authority and the Auditor-General
• the audit committee must communicate any concerns it deems necessary to the executive authority, the Auditor-General and if appropriate, to the external auditor
• the audit committee must meet at least annually with the Auditor-General or the external auditor, whichever applicable, to ensure that there are no unresolved issues of concern

The audit committee of a Public Entity must, amongst others, review the following:
• the effectiveness of the internal control systems
• the effectiveness of internal audit
• the risk areas of the entity’s operations to be covered in the scope of internal and external audits
• the adequacy, reliability and accuracy of financial information provided to management and other users of such information
• any accounting and auditing concerns identified as a result of internal and external audits
• the entity’s compliance with legal and regulatory provisions
• the activities of the internal audit function, including its annual work programme, coordination with the external auditors, the reports of significant investigations and the responses of management to specific recommendations

• where relevant, the independence and objectivity of the external auditors.

The audit committee of a Public Entity must –
• report and make recommendations to the accounting authority
• report on the effectiveness of internal controls in the integrated report of the institution
• comment on its evaluation of the financial statements in the annual report.

Similar to the requirements of the PFMA on the Accounting Authorities of Public Entities to establish audit committees, the Municipal Finance Management Act (MFMA), does also require the establishment of audit committees in terms of its section 166 (1) which states that each municipality and each municipal entity must have an audit committee. A single audit committee may be established for a district municipality and the local municipalities within that district municipality; or a municipality and municipal entities under its sole control.
The members of an audit committee must be appointed by the council of the municipality or, in the case of a municipal entity, by the council of the parent municipality. One of the members, who is not in the employ of the municipality or municipal entity, must be appointed as the chairperson of the committee. No councillor may be a member of an audit committee. An audit committee of a municipality must:
• consist of at least three persons with appropriate experience, of whom the majority may not be in the employ of the municipality or municipal entity, as the case may be
• meet as often as is required to perform its functions, but at least four times a year.

In terms of the MFMA an audit committee is an independent advisory body which must:
• advise the municipal council, the political office-bearers, the accounting officer and the management staff of the municipality, or the board of directors, the accounting officer and the management staff of the municipal entity, on matters relating to—
  - internal financial control and internal audits
  - risk management
  - accounting policies
  - the adequacy, reliability and accuracy of financial reporting and information
  - performance management
  - effective governance
• compliance with this Act, the annual Division of Revenue Act and any other applicable legislation
• performance evaluation
• any other issues referred to it by the municipality or municipal entity.
• review the annual financial statements to provide the council of the municipality or, in the case of a municipal entity, the council of the parent municipality and the board of directors of the entity, with an authoritative and credible view of the financial position of the municipality or municipal entity, its efficiency and effectiveness and its overall level of compliance with this MFMA, the annual Division of Revenue Act and any other applicable legislation
• respond to the council on any issues raised by the Auditor-General in the audit report
• carry out such investigations into the financial affairs of the municipality or municipal entity as the council of the municipality, or in the case of a municipal entity, the council of the parent municipality or the board of directors of the entity, may request.
In performing its functions, an audit committee:
  • has access to the financial records and other relevant information of the municipality or municipal entity
  • must liaise with:
    - the internal audit unit of the municipality
    - the person designated by the Auditor-General to audit the financial statements of the municipality or municipal entity.

A shared audit committee may be established for a public entity and any subsidiaries under the ownership and control of that entity.
Contacts

Dr Johan Erasmus
Tel: 082 573 2536
jerasmus@deloitte.co.za

Nina le Riche
Tel: 082 331 4840
nleriche@deloitte.co.za
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