



FINANCIAL REPORTING COUNCIL

**2010 CONSULTATION ON REVISIONS TO
THE FRC GUIDANCE ON AUDIT COMMITTEES**

SUMMARY OF RESPONSES TO THE CONSULTATION

DECEMBER 2010

CONSULTATION ON FRC GUIDANCE ON AUDIT COMMITTEES: SUMMARY OF RESPONSES

Introduction

1. In July 2010 the FRC consulted on limited amendments to the FRC Guidance on Audit Committees, arising from work undertaken by the FRC's Auditing Practices Board (APB) on the provision of non-audit services and audit partner rotation. The consultation was carried out in parallel with a consultation on revisions to the Ethical Standards for Auditors. Both consultations ended in October 2010.
2. Nineteen submissions were received. Respondents are listed in Appendix A to this document, with the exception of one organisation who asked that their views be considered private. Copies of the submissions are available at: <http://www.frc.org.uk/corporate/response-auditcommittees.cfm>. In addition, a small number of organisations that did not respond to this consultation made comments that were relevant to the guidance in their responses to the separate consultation on the Ethical Standards. Those comments have also been taken into account.
3. All respondents supported the broad thrust of the proposed amendments, with the exception of one FTSE Small Cap company that considered them to be burdensome and unnecessary. Some respondents commented on the detail of the proposed changes. This document summarises those comments and explains how the FRC has responded to them. Appendix B shows how Section 4 of the guidance has been amended as a result of the consultation process.

Proposed changes to the guidance

4. The changes proposed to the Guidance on Audit Committees in the July consultation document can be summarised as follows:
 - More prominence was given to the importance of non-audit services in the assessment of the objectivity and independence of the company's auditor by moving the guidance currently in paragraphs 4.28 and 4.29 to later in the document (revised paragraphs 4.34 and 4.35);
 - A number of corporate respondents to the APB's October 2009 consultation on non-audit services suggested that the practice of seeking specific approval from audit committees for particular categories and values of non-audit services to be supplied by the auditor was widely followed. This type of policy and procedure was set out in paragraph 4.30.

- Additional guidance was given in paragraph 4.31 to help the audit committee distinguish between those non-audit services which are closely related to an audit and which give rise to a very low threat to auditor objectivity and those where the threats need more careful consideration. This is consistent with the identification of 'audit related services' as a separate category of non-audit services proposed in the APB's Ethical Standards for Auditors. A number of corporate respondents to the earlier consultation thought that disclosing the nature of the services provided (particularly where they are similar to an audit) would allay fears that the auditor is conflicted by the purchase of such non-audit services and therefore help maintain confidence in the quality of the audit.
- It is thought that by identifying audit related services, there will be a greater focus on other non-audit services by both audit committees and investors. There is no presumption that services in this third category are services that the entity's auditor should not provide. A judgment needs to be made by audit committees as to the cost and efficiency benefits and the real or perceived threats to auditor independence which are associated with the auditor providing them. Guidance on such judgments was given in paragraph 4.32.
- Improved disclosures of the audit committee policy, as set out in paragraph 4.38, would give more detail on the nature of services provided by the auditor and will outline the reasons why the audit committee decided to purchase non-audit services, other than audit related services, from the auditor rather than from another party. This increased transparency will enable investors to monitor the judgments made by audit committees and to make it known where they disagree.
- Although not directly linked to greater transparency, there were two other amendments proposed to the Guidance on Audit Committees which are connected with the APB Ethical Standards for Auditors:
 - Additional guidance on factors to take into account when the external auditor is being considered to provide internal audit services was added in paragraph 4.8.
 - Additional guidance on flexibility that is available in respect of the rotation of the audit engagement partner was provided in paragraph 4.36.

Comments on the proposed changes and the FRC's response

Provision of non-audit services

5. Eight respondents commented on the proposed changes in paragraphs 4.29 to 4.33.
6. One respondent considered that the recommendation in paragraph 4.29 for the committee to consider whether the external auditor was a suitable supplier of the non-audit service should be strengthened, arguing that the test should be whether the external auditor was more suitable than other suppliers. The FRC considers that this change would better reflect its original intent, as reflected in the wording of paragraph 4.38 that the audit committee should consider why "it was in the interests of the company to purchase them [the non-audit service] from the external auditor (rather than another supplier)", and has amended paragraph 4.29 accordingly.
7. One respondent considered that assessments of the external auditor's independence and objectivity should take place every year and before approval of any non-audit work. The FRC considers this would be too prescriptive but agrees that these matters should be kept under review by the committee and has added wording to this effect in paragraph 4.29.
8. A few respondents considered that paragraphs 4.31 and 4.33 should summarise the relevant parts of the Ethical Standards rather than expect audit committees to cross-refer to them. The FRC accepts this point, and has expanded the related footnotes accordingly.
9. A couple of respondents considered that it was not helpful to use terminology such as "routine in nature" and "not significant" in paragraph 4.31, and that clearer terms should be used. While the FRC understands this concern, it believes that it would be difficult to be clearer without becoming more prescriptive, which it does not wish to do as these questions should be for the audit committee to judge. Accordingly no further change has been made to paragraph 4.31.
10. Two respondents to the consultation on the Ethical Standards considered that the reference in paragraph 4.32 to "how this [the non-audit service] will be disclosed in the annual report" implied that all individual services would have to be disclosed, which was inconsistent with the wording in paragraph 4.38. The FRC agrees, and has deleted the wording in paragraph 4.32.

11. Other suggestions put forward that have not been acted on include:

- That audit committees should also consider to which companies in a group the policy on non-audit services should apply. The FRC considers that the existing references in paragraph 1.12 of the guidance to the duties of the parent company's audit committee should suffice.
- That the recommendation in paragraph 4.31 that engagements should be both routine in nature and not significant in the context of the audit fee in order to be pre-approved was too restrictive. The FRC does not agree with this view.
- That paragraph 4.32 should be amended to make it clear that there is no presumption against the external auditor carrying out non-audit services. The FRC considers that the guidance is already sufficiently clear on this point.

Disclosure on non-audit services

12. Ten respondents commented on the recommended disclosures in paragraph 4.38.

13. While all agreed that clearer disclosure about the policy on non-audit services and how it had been applied was useful, many of them expressed the concern that including all the recommended information in the annual report could significantly add to its length. The FRC accepts this concern, and agrees that the description of the policy on engagement of the external auditor to carry out non-audit services, which is unlikely to change significantly from year to year, could appropriately be disclosed on the company's website. On the other hand, the FRC considers that information on how the committee has applied the policy in practice will be different every year, and likely to be of considerable interest to shareholders, and should therefore be included in the annual report. Paragraph 4.38 has been amended accordingly.

14. In addition, the footnote to paragraph 4.38 has been expanded to clarify that the disclosure of the fees paid to the auditor can cross-refer to the existing statutory requirement to disclose this information, and therefore will not add to the length of the report.

15. Several respondents considered that the recommendation that the committee disclose the reasons why it considered it appropriate for the external auditor to be awarded each “significant engagement” could lead to lengthy disclosure, and some requested that further guidance be given on how significance should be defined. While the FRC understands this concern, it believes that it would be difficult to be clearer without becoming more prescriptive, which it does not wish to do as these questions should be for the audit committee to judge. Accordingly no further change has been made.

16. Other suggestions put forward that have not been acted on include:

- Two respondents suggested further disclosures, some of which are already addressed in other parts of the guidance. The FRC considers that the recommendations in paragraph 4.38 strike the right balance.
- One respondent expressed the concern that the categories against which companies were being recommended to report were not consistent with those required under the Companies (Disclosure of Auditor Remuneration and Liability Limitation Agreements) Regulations 2008. Other respondents also raised a similar point in response to the APB’s consultation on the Ethical Standards. The template for the provision of this information by the auditors to the audit committee in Ethical Standard 1 has been amended in response to this point and could be used by companies for reporting purposes, as the footnote to paragraph 4.38 now makes clear.

Internal audit

17. Six respondents commented on the proposed new paragraph 4.8 on the issues to be considered if the external auditor was being considered to undertake aspects of the internal control function. A number of them noted concerns about the potential impact on the independence and objectivity of both the internal audit function and the external auditor, and felt that this should be given more prominence in the guidance. The FRC agrees with these points, and has added an additional bullet point to paragraph 4.8 to emphasise the need to ensure that independence and objectivity have been safeguarded.

18. One respondent suggested that the guidance should be expanded to state that audit committees should satisfy themselves that the division of responsibility of functions between the internal audit and external auditor was appropriate, and report on this to shareholders. The FRC considers that the recommended disclosures in paragraph 4.38 adequately address this point.

19. One respondent suggested that there should be a clear presumption against the external auditor carrying out internal audit functions, and one suggested that further references should be added to paragraph 4.32 to illustrate how the general policy on non-audit services would be applied where the external auditor was being considered to undertake some internal audit functions. The FRC has made no change to the guidance in response to these comments.

Rotation of audit partners

20. There were no substantive comments on the proposed amendments to paragraph 4.36 of the guidance; therefore no further changes have been made.

Financial Reporting Council
December 2010

APPENDIX A

RESPONDENTS TO THE JULY 2010 CONSULTATION

Note: this list excludes one organisation that requested that its response remain private.

ACCA
Amec plc
Association of British Insurers
British American Tobacco plc
BT Group plc
CBI
Chartered Institute of Internal Auditors
Ernst & Young LLP
GC100 Group
Hermes Equity Ownership Service
Institute of Chartered Accountants of Scotland
International Corporate Governance Network
KPMG LLP
PayPoint plc
PricewaterhouseCoopers LLP
Quoted Companies Alliance
Standard Life plc
UK Shareholders Association

REVISED GUIDANCE ON AUDIT COMMITTEES

Note: Changes proposed in the July 2010 consultation document are shown in underlined and strike-through text. Additional changes proposed as a result of the consultation are shown in bold and italics.

4 Role and responsibilities

Financial reporting

- 4.1 The audit committee should review the significant financial reporting issues and judgements made in connection with the preparation of the company's financial statements, interim reports, preliminary announcements and related formal statements.
- 4.2 It is management's, not the audit committee's, responsibility to prepare complete and accurate financial statements and disclosures in accordance with financial reporting standards and applicable rules and regulations. However the audit committee should consider significant accounting policies, any changes to them and any significant estimates and judgements. The management should inform the audit committee of the methods used to account for significant or unusual transactions where the accounting treatment is open to different approaches. Taking into account the external auditor's view, the audit committee should consider whether the company has adopted appropriate accounting policies and, where necessary, made appropriate estimates and judgements. The audit committee should review the clarity and completeness of disclosures in the financial statements and consider whether the disclosures made are set properly in context.
- 4.3 Where, following its review, the audit committee is not satisfied with any aspect of the proposed financial reporting by the company, it shall report its views to the board.
- 4.4 The audit committee should review related information presented with the financial statements, including the operating and financial review, and corporate governance statements relating to the audit and to risk management. Similarly, where board approval is required for other statements containing financial information (for example, summary financial statements, significant financial returns to regulators and release of price sensitive information), whenever practicable (without being inconsistent with any requirement for prompt reporting under the Listing Rules) the audit committee should review such statements first.

Internal controls and risk management systems

- 4.5 The audit committee should review the company's internal financial controls (that is, the systems established to identify, assess, manage and monitor financial risks); and unless expressly addressed by a separate board risk committee comprised of independent directors or by the board itself, the company's internal control and risk management systems.
- 4.6 The company's management is responsible for the identification, assessment, management and monitoring of risk, for developing, operating and monitoring the system of internal control and for providing assurance to the board that it has done so. Except where the board or a risk committee is expressly responsible for reviewing the effectiveness of the internal control and risk management systems, the audit committee should receive reports from management on the effectiveness of the systems they have established and the conclusions of any testing carried out by internal and external auditors.
- 4.7 Except to the extent that this is expressly dealt with by the board or risk committee, the audit committee should review and approve the statements included in the annual report in relation to internal control and the management of risk.
- 4.8 If the external auditor is being considered to undertake aspects of the internal audit function, the audit committee should consider the effect this may have on the effectiveness of the company's overall arrangements for internal control and investor perceptions in this regard. Investor perceptions are likely to be influenced by:
- the rationale set out in the annual report for the work being performed by the external auditor;
 - the nature and extent of the work performed by the external auditor;
 - *how the independence and objectivity of the external auditor and internal audit function have been safeguarded;* and
 - whether, in the absence of internal audit work, the audit committee is wholly reliant on the views of the external auditor about the effectiveness of its system of controls relating to core activities and significant locations.

Whistleblowing

- 4.9 **The audit committee should review arrangements by which staff of the company may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters. The audit committee's objective should be to ensure that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action.**

The internal audit process

- 4.10 **The audit committee should monitor and review the effectiveness of the company's internal audit function. Where there is no internal audit function, the audit committee should consider annually whether there is a need for an internal audit function and make a recommendation to the board, and the reasons for the absence of such a function should be explained in the relevant section of the annual report.**
- 4.11 The need for an internal audit function will vary depending on company specific factors including the scale, diversity and complexity of the company's activities and the number of employees, as well as cost/benefit considerations. Senior management and the board may desire objective assurance and advice on risk and control. An adequately resourced internal audit function (or its equivalent where, for example, a third party is contracted to perform some or all of the work concerned) may provide such assurance and advice. There may be other functions within the company that also provide assurance and advice covering specialist areas such as health and safety, regulatory and legal compliance and environmental issues.
- 4.12 When undertaking its assessment of the need for an internal audit function, the audit committee should also consider whether there are any trends or current factors relevant to the company's activities, markets or other aspects of its external environment, that have increased, or are expected to increase, the risks faced by the company. Such an increase in risk may also arise from internal factors such as organisational restructuring or from changes in reporting processes or underlying information systems. Other matters to be taken into account may include adverse trends evident from the monitoring of internal control systems or an increased incidence of unexpected occurrences.
- 4.13 In the absence of an internal audit function, management needs to apply other monitoring processes in order to assure itself, the audit committee and the board that the system of internal control is functioning as intended. In these circumstances, the audit committee will need to assess whether such processes provide sufficient and objective assurance.

- 4.14 The audit committee should review and approve the internal audit function's remit, having regard to the complementary roles of the internal and external audit functions. The audit committee should ensure that the function has the necessary resources and access to information to enable it to fulfil its mandate, and is equipped to perform in accordance with appropriate professional standards for internal auditors¹.
- 4.15 The audit committee should approve the appointment or termination of appointment of the head of internal audit.
- 4.16 In its review of the work of the internal audit function, the audit committee should, inter alia:
- ensure that the internal auditor has direct access to the board chairman and to the audit committee and is accountable to the audit committee;
 - review and assess the annual internal audit work plan;
 - receive a report on the results of the internal auditors' work on a periodic basis;
 - review and monitor management's responsiveness to the internal auditor's findings and recommendations;
 - meet with the head of internal audit at least once a year without the presence of management; and
 - monitor and assess the role and effectiveness of the internal audit function in the overall context of the company's risk management system.

The external audit process

- 4.17 The audit committee is the body responsible for overseeing the company's relations with the external auditor.

Appointment

- 4.18 The audit committee should have primary responsibility for making a recommendation on the appointment, reappointment and removal of the external auditors. If the board does not accept the audit committee's recommendation, it should include in the annual report, and in any papers recommending appointment or reappointment, a statement from the audit committee explaining its recommendation and should set out reasons why the board has taken a different position.**

¹ Further guidance can be found in the Chartered Institute of Internal Auditors' Code of Ethics and the International Standards for the Professional Practice of Internal Auditing.

- 4.19 The audit committee's recommendation to the board should be based on the assessments referred to below. If the audit committee recommends considering the selection of possible new appointees as external auditors, it should oversee the selection process.
- 4.20 The audit committee should assess annually the qualification, expertise and resources, and independence (see paragraph 4.27 below) of the external auditors and the effectiveness of the audit process. The assessment should cover all aspects of the audit service provided by the audit firm, and include obtaining a report on the audit firm's own internal quality control procedures and consideration of audit firms' annual transparency reports, where available. It might also be appropriate for the audit committee to consider whether there might be any benefit in using firms from more than one audit network².
- 4.21 If the external auditor resigns, the audit committee should investigate the issues giving rise to such resignation and consider whether any action is required.
- 4.22 The audit committee should consider the need to include the risk of the withdrawal of their auditor from the market in their risk evaluation and planning.
- 4.23 The audit committee section of the annual report should explain to shareholders how it reached its recommendation to the board on the appointment, reappointment or removal of the external auditors. This explanation should normally include supporting information on tendering frequency, the tenure of the incumbent auditor, and any contractual obligations that acted to restrict the audit committee's choice of external auditors.

Terms and Remuneration

- 4.24 The audit committee should approve the terms of engagement and the remuneration to be paid to the external auditor in respect of audit services provided.
- 4.25 The audit committee should review and agree the engagement letter issued by the external auditor at the start of each audit, ensuring that it has been updated to reflect changes in circumstances arising since the previous year. The scope of the external audit should be reviewed by the audit committee with the auditor. If the audit committee is not satisfied as to its adequacy it should arrange for additional work to be undertaken.

² Guidance on the considerations relevant to the use of firms from more than one audit network can be found in the Appendix.

- 4.26 The audit committee should satisfy itself that the level of fee payable in respect of the audit services provided is appropriate and that an effective audit can be conducted for such a fee.

Independence, including the provision of non-audit services

- 4.27 The audit committee should assess the independence and objectivity of the external auditor annually, taking into consideration relevant UK law, regulation and professional requirements. This assessment should involve a consideration of all relationships between the company and the audit firm (including the provision of non-audit services) and any safeguards established by the external auditor. The audit committee should consider whether, taken as a whole and having regard to the views, as appropriate, of the external auditor, management and internal audit, those relationships appear to impair the auditor's independence and objectivity.
- 4.28 The audit committee should seek reassurance that the auditors and their staff have no financial, business, employment or family and other personal relationship with the company which could adversely affect the auditor's independence and objectivity, taking account of relevant Ethical Standards. The audit committee should seek from the audit firm, on an annual basis, information about policies and processes for maintaining independence and monitoring compliance with relevant requirements, including current requirements regarding the rotation of audit partners and staff.
- 4.29 The audit committee should develop and recommend to the board the company's policy in relation to the provision of non-audit services by the auditor, *and keep the policy under review*. The audit committee's objective should be to ensure that the provision of such services does not impair the external auditor's independence or objectivity. In this context, the audit committee should consider:
- whether the skills and experience of the audit firm make it *the most* suitable supplier of the non-audit service;
 - whether there are safeguards in place to eliminate or reduce to an acceptable level any threat to objectivity and independence in the conduct of the audit resulting from the provision of such services by the external auditor;
 - the nature of the non-audit services;
 - the fees incurred, or to be incurred, for non-audit services both for individual services ~~related fee levels and the fee levels individually~~ and in aggregate, relative to the audit fee; and
 - the criteria which govern the compensation of the individuals performing the audit.

4.30 The audit committee should set and apply a formal policy specifying the types of non-audit service work (if any):

- ~~from which the external auditors are excluded;~~
- for which the use of the external auditor is pre-approved (i.e. approval has been given in advance as a matter of policy, rather than the specific approval of an engagement being sought before it is contracted) can be engaged without referral to the audit committee; and;
- for which specific approval from the audit committee is required before they are contracted; and
- from which the external auditor is excluded.

~~In addition the policy may set fee limits generally or for particular classes of work.~~

4.31 Pre-approval of the use of the external auditor may be appropriate where the threats to auditor independence are considered low, for example if the engagement is:

- routine in nature and the fee is ~~very small~~ not significant in the context of the audit fee; or
- for an audit related service.³

4.32 ~~In the third category, if it is not practicable to give approval to individual items in advance, it may be appropriate to give a general pre-approval for certain classes for work, subject to a fee limit determined by the audit committee and ratified by the board. The subsequent provision of any service by the auditor should be ratified at the next meeting of the audit committee. The non-audit services that fall within the second category in paragraph 4.30 above are likely to be those which, because of their size or nature or because of special terms and conditions (for example, contingent fee arrangements), are thought to give rise to threats to the auditor's independence. As a consequence, careful consideration will be needed when determining whether it is in the interests of the company that they should be purchased from the audit firm (rather than another~~

³ Audit related services are those non-audit services specified as such in APB Ethical Standards for Auditors as including:

- Reporting required by law or regulation to be provided by the auditor;
- Reviews of interim financial information;
- Reporting on regulatory returns;
- Reporting to a regulator on client assets;
- Reporting on government grants;
- Reporting on internal financial controls when required by law or regulation;
- Extended work that is authorised by those charged with governance on financial information and/or financial controls performed where this work is integrated with the audit work and is performed on the same principal terms and conditions.

supplier) and, if so, whether any safeguards to be put in place by the audit firm are likely to be effective, ~~and how this will be disclosed in the annual report~~ [deleted from consultation draft].

4.33 In determining the policy, the audit committee should take into account the possible threats to auditor objectivity and independence⁴ and APB relevant Ethical Standards for Auditors regarding the provision of non-audit services by the external audit firm. ~~and in principle should not agree to the auditor providing a service if, having regard to the ethical guidance, the result is that:~~

- ~~• the external auditor audits its own firm's work;~~
- ~~• the external auditor makes management decisions for the company;~~
- ~~• a mutuality of interest is created;~~
- ~~• the external auditor develops close personal relationships with the company's personnel; or~~
- ~~• the external auditor is put in the role of advocate for the company.~~

~~The audit committee should satisfy itself that any safeguards required by Ethical Standards are implemented.~~

4.34 The audit committee should agree with the board the company's policy for the employment of former employees of the external auditor, taking into account the APB Ethical Standards for Auditors paying particular attention to the policy regarding former employees of the audit firm who were part of the audit team and moved directly to the company. The audit committee should monitor application of the policy, including the number of former employees of the external auditor currently employed

⁴ APB Ethical Standards for Auditors explain that threats to auditor objectivity and independence may arise from:

- Self-interest threats which arise when the auditor has financial or other interests which might cause it to be reluctant to take actions that would be adverse to the interests of the audit firm or any individual in a position to influence the conduct and outcome of the audit;
- Self-review threats which arise when the results of a non-audit service performed by the auditor or others within the firm are reflected in the amounts included or disclosed in the financial statements of the audited entity;
- Management threats which arise where partners and employees of the audit firm make judgments or take decisions on behalf of the management of the audited entity;
- Advocacy threats which arise when the audit firm undertakes work that involves acting as an advocate for an audited entity and supporting a position taken by management in an adversarial context;
- Familiarity threats which arise when the auditor is predisposed to accept or is insufficiently questioning of the audited entity's point of view; and
- Intimidation threats which arise when the auditor's conduct is influenced by fear or threats.

in senior positions in the company, and consider whether in the light of this there has been any impairment, or appearance of impairment, of the auditor's independence and objectivity in respect of the audit. (*Current paragraph 4.28*)

4.35 The audit committee should monitor the external audit firm's compliance with APB Ethical Standards for Auditors relating to the rotation of audit partners, the level of fees that the company pays in proportion to the overall fee income of the firm, or relevant part of it⁵, and other related regulatory requirements. (*Current paragraph 4.29*)

4.36 A degree of flexibility over the timing of rotation of the audit engagement partner is possible where the audit committee decides that it is necessary to safeguard the quality of the audit. In such circumstances, the audit engagement partner may continue in this position for an additional period of up to two years, so that no longer than seven years in total is spent in this position. The audit committee should disclose this fact and the reasons for it to the shareholders as early as practicable.

4.37 The annual report should explain to shareholders how, if the auditor provides non-audit services, auditor objectivity and independence is safeguarded.

4.38 The explanation should:

- describe the work of the committee in discharging its responsibilities;
- set out the audit committee's policy on the engagement of the external auditor to supply non-audit services in sufficient detail to describe each of the elements in paragraph 4.30, or cross-refer to where this information can be found on the company's website;
- set out, or cross refer to, the fees paid to the auditor for audit services, audit related services and other non-audit services⁶; and
- if the auditor provides non-audit services, other than audit related services, explain for each significant engagement, or category of engagements, what the services are, why the audit committee concluded that it was in the interests of the company to purchase them from the external auditor (rather than another supplier) and how auditor objectivity and independence has been safeguarded.

⁵ Where the audit firm's profits are not shared on a firm-wide basis, the relevant part of the firm is that by reference to which the audit engagement partner's profit share is calculated.

⁶ *The statutory requirement for disclosure in the financial statements is contained in the Companies (Disclosure of Auditor Remuneration and Liability Limitation Agreements) Regulations 2008. A template for the provision of this information by the auditors to the audit committee is set out in Appendix A to Ethical Standard 1 issued by the Auditing Practices Board.*

Annual audit cycle

- 4.39 At the start of each annual audit cycle, the audit committee should ensure that appropriate plans are in place for the audit.
- 4.40 The audit committee should consider whether the auditor's overall work plan, including planned levels of materiality, and proposed resources to execute the audit plan appears consistent with the scope of the audit engagement, having regard also to the seniority, expertise and experience of the audit team.
- 4.41 The audit committee should review, with the external auditors, the findings of their work. In the course of its review, the audit committee should:
- discuss with the external auditor major issues that arose during the course of the audit and have subsequently been resolved and those issues that have been left unresolved;
 - review key accounting and audit judgements; and
 - review levels of errors identified during the audit, obtaining explanations from management and, where necessary, the external auditors as to why certain errors might remain unadjusted.
- 4.42 The audit committee should also review the audit representation letters before signature by management and give particular consideration to matters where representation has been requested that relate to non-standard issues⁷. The audit committee should consider whether the information provided is complete and appropriate based on its own knowledge.
- 4.43 As part of the ongoing monitoring process, the audit committee should review the management letter (or equivalent). The audit committee should review and monitor management's responsiveness to the external auditor's findings and recommendations.
- 4.44 At the end of the annual audit cycle, the audit committee should assess the effectiveness of the audit process. In the course of doing so, the audit committee should:
- review whether the auditor has met the agreed audit plan and understand the reasons for any changes, including changes in perceived audit risks and the work undertaken by the external auditors to address those risks;
 - consider the robustness and perceptiveness of the auditors in their handling of the key accounting and audit judgements identified and in responding to questions from the audit committees, and in

⁷ Further guidance can be found in the Auditing Practices Board's International Standard on Auditing (UK and Ireland) 580: "Management Representations".

their commentary where appropriate on the systems of internal control;

- obtain feedback about the conduct of the audit from key people involved, e.g. the finance director and the head of internal audit; and
- review and monitor the content of the external auditor's management letter, in order to assess whether it is based on a good understanding of the company's business and establish whether recommendations have been acted upon and, if not, the reasons why they have not been acted upon.

Consequential amendment to paragraph 5.2

The audit committee section should include, inter alia:

- a summary of the role of the audit committee;
- the names and qualifications of all members of the audit committee during the period;
- the number of audit committee meetings;
- a report on the way the audit committee has discharged its responsibilities; and
- the explanations provided for in paragraphs ~~4.22 and 4.34~~ 4.23 and 4.37 above.



FINANCIAL REPORTING COUNCIL
5TH FLOOR
ALDWYCH HOUSE
71-91 ALDWYCH
LONDON WC2B 4HN
TEL: +44 (0)20 7492 2300
FAX: +44 (0)20 7492 2301
WEBSITE: www.frc.org.uk

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