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Audit committee resource guide

MAKING AN IMPACT THAT MATTERS since 1845

References

The King IV Report on Corporate Governance for South Africa 2016 (King IV)

Companies Act 71 of 2008

JSE Listings Requirements

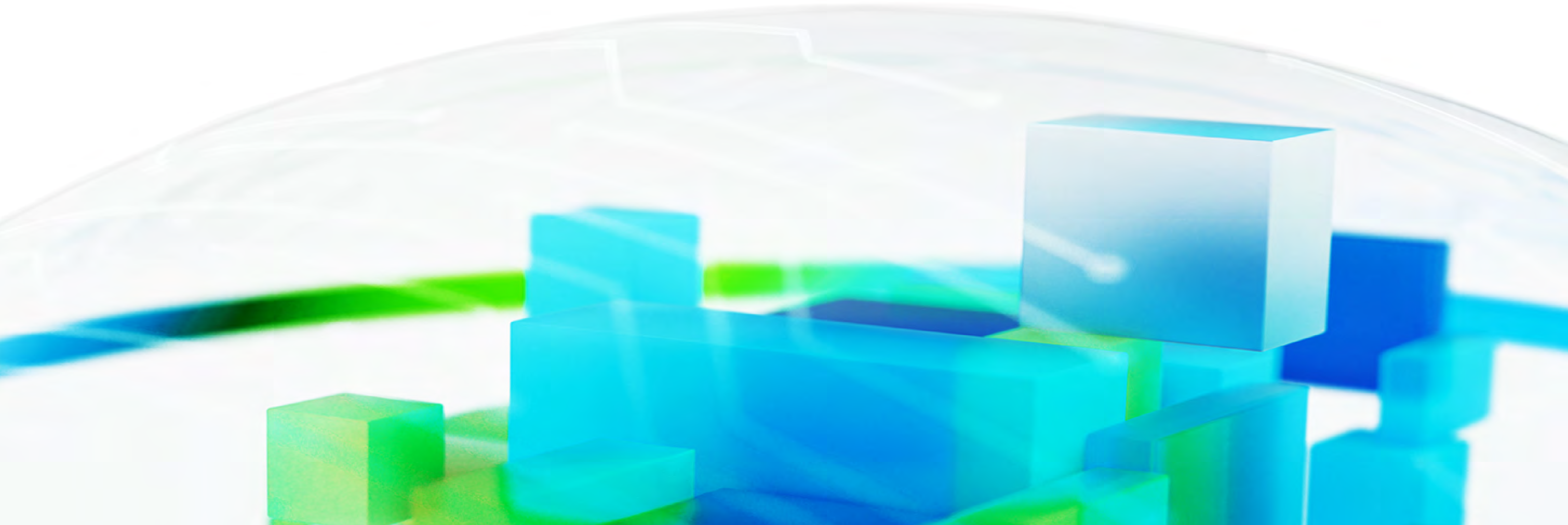
The SAICA Guide to the Companies Act (only available to members of SAICA)

Financial Reporting Council (UK) Guidance on Audit Committees

Code of Professional Conduct for Registered Auditors

Auditing Profession Act

IIA's Standards for Professional Practice of Internal Auditing(UK)



Contents

Key

Company and entity will be used interchangeably and will apply to both except if ***Companies Act*** specific.

Legislation

This box indicates legislation or statutory requirements

South Africa specific legislation/requirements

Questions to consider

Tips, checklists and recommendations

Click on hyperlink

ACTION ITEMS

Section 1: Audit committee leading practices and trends

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, to discuss committee agenda items 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
- Conduct an annual committee self-evaluation
- Consider periodically rotating audit committee members, including the chair
- Encourage discussion, rather than presentation, at meetings
- Participate in Audit Committee education activities
- Engage independent advisers when needed
- Meet at least quarterly, or more frequently as circumstances dictate
- Maintain appropriate coordination between the Audit Committee and other board committees

Self-assessment and evaluation of effectiveness

- Review and approve the Audit Committee charter and align activities with a calendar that incorporates required activities and allows flexibility for additional topics
- Develop meeting agendas in consultation with management; resist the urge to repurpose existing agendas without discussion
- Align Audit Committee meeting materials and agendas with priority areas
- Distribute briefings and other materials well in advance of meetings
- Reports should include executive summaries that highlight issues and critical discussion points to allow for discussion versus presentation during meetings
- Manage meeting attendees to allow open and candid discussions
- Perform a robust self-assessment performance evaluation annually (**Appendix C**)
- Discuss the results of the self-assessment with the Audit Committee in an executive session and develop tactical actions to address findings

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 external 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 judgements 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 and integrated reporting may affect the company, particularly its talent needs

Risk oversight

- Focus on financial risks, fraud risk and other risks that may affect the integrity of external reports
- 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 risk
- Evaluate information technology (IT) projects (with a focus on financial reporting), including IT milestones and reporting against them, especially for IT transformation
- 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

Interaction with the external auditor

- Exercise ownership of the relationship with the external 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 external auditor
- Focus on the external auditor's qualifications, performance, independence, and compensation, including a pre-approval process for audit and non-audit services
- Provide formal evaluations and regular feedback
- Request and evaluate inspection results from regulators and consider audit quality indicators, if available

Reminder

The onus of the eligibility of the auditor rests solely on the audit committee.

Partnership with the CFO and other management

- Focus on the tone at the top, culture, ethics, and hotline monitoring
- Conduct annual evaluations of the CFO
- 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

- Audit Committee meetings should be preceded or followed by private sessions with the CFO, the internal auditors, and the external auditor
- Use an executive session for committee members to discuss how the meeting went and to identify agenda topics for future meetings
- Discuss succession plans for the finance organisation with the CEO and CFO annually during a private session
- Establish expectations as to what sort of topics and discussions are expected of the external auditor in private sessions

Executive compensation

- Coordinate with the remuneration committee on incentive compensation goals
- Work with the remuneration committee to understand the implications of the incentive structure, including its impact on employee retention and potential increases in fraud risk
- Increase focus on the compensation of officers and directors, including the appropriate use of corporate assets

Interaction with the internal auditors

- Ensure that the internal auditors have direct access to the Audit Committee
- Consider having internal audit report directly to the Audit Committee and administratively to senior management
- Play an active role in determining the highest and best use of internal audit, as well as the appropriate structure of the group (e.g., in-house versus outsourced resources)
- Be involved with the internal audit risk assessment and audit plans, including activities and objectives regarding internal control over financial reporting
- Conduct annual evaluations of the chief audit executive
- Understand internal audit staffing, funding, and succession planning, particularly the adequacy of resources; consider performing peer benchmarking to compare relevant metrics

Orientation and continuing education

- Address board education in the company's corporate governance guidelines to be consistent with the ***JSE Listings Requirements***
- Provide orientation of new members that involves company executives, internal audit, and the external auditor
- Include educational topics on the agendas 1-2 times per year; topics may include: a deep dive on a specific area of the business and related risks, or a refresher on a significant accounting estimate
- Consider offering annual continuing education opportunities in financial reporting and other areas relevant to the Audit Committee (e.g., specialised or regulated industry matters, new regulations, operations, and emerging topics such as cybersecurity and ESG (Environmental, Social & Governance))

Legal or non-compliance matters

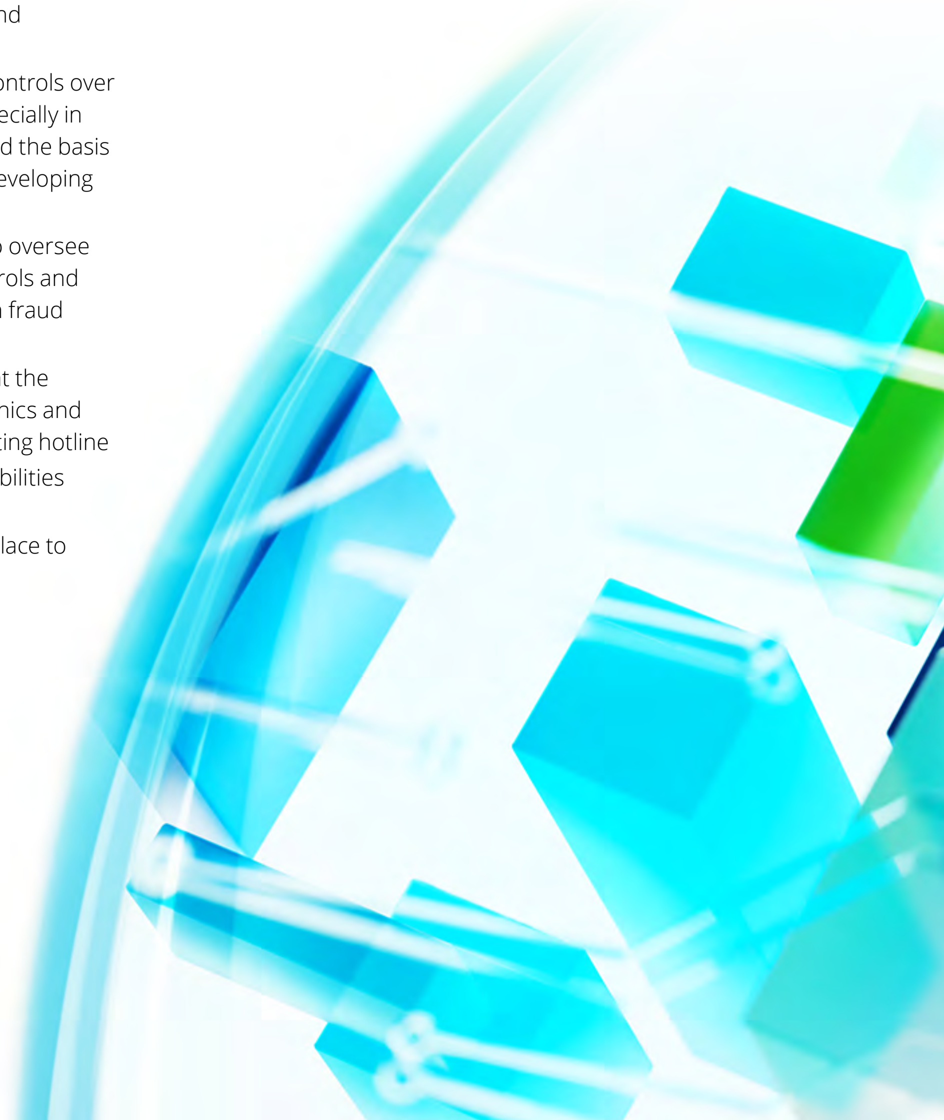
- Consider how the company ensures compliance with legal and regulatory requirements which could directly or indirectly affect the entity's operations, risks, reputation and financial statements
- Consider new regulations and best practices (for example sustainability disclosures) that the entity may need to comply with now or in the future
- The committee should meet periodically in executive sessions with those responsible for overseeing ethics and compliance matters and work with management to confirm that the company's code of ethics or conduct complies with the applicable requirements

Related parties and conflict of interest

- Consider the need to review and oversee related-party relationships and transactions by a member of the committee or by the committee itself
- Ensure sufficient oversight of related party transactions, especially those involving entities affiliated with a director or key management and their family members
- Remain alert for any dealings which may give rise to conflicts of interest

Fraud considerations

- Committee members should be aware of three main areas of fraud risk being financial statement fraud, asset misappropriation and corruption
- Ensure management have appropriate policies and procedures in place to prevent and detect fraud
- Monitor management's assessment of internal controls over fraud and the financial reporting framework, especially in relation to the selection of accounting policies and the basis of the methods, assumptions and data used in developing accounting estimates
- The committee should work with management to oversee the establishment of appropriate anti-fraud controls and programmes and to take appropriate steps when fraud is detected
- The Audit Committee should also be satisfied that the organisation has implemented an appropriate ethics and compliance programme and established a reporting hotline
- Understand the entity's obligations and responsibilities regarding anti-corruption and money laundering
- Understand specific policies and procedures in place to identify and mitigate corruption-related risks



Section 2: Audit committee composition

Section 2: Audit committee composition

The King IV Report on Corporate Governance for South Africa 2016 (King IV) emphasises the vital role of an audit committee in ensuring the effectiveness of the organisation's assurance functions and services, with particular focus on combined assurance arrangements, including external assurance service providers, internal audit and the finance function, and the integrity of the annual financial statements and other external reports issued by the organisation. The key role of the audit committee is echoed in the ***Companies Act, 2008 (Act No 71 of 2008) (the Companies Act)*** and the ***JSE Listings Requirements***.

Appointment of the audit committee

The ***Companies Act*** requires public companies and state-owned companies to appoint an audit committee. In addition, any other type of company (private company, personal liability company or non-profit company) that provides for the appointment of an audit committee in their Memorandum of Incorporation must comply with the relevant provisions of the ***Companies 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 IV*** proposes that ALL companies should have an audit committee. In terms of the ***JSE Listings Requirements*** the appointment of the committee should be considered in accordance with the recommended practices in the ***King Code*** on an apply or explain basis, provided that each committee must comprise of at least three members.

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. The audit committee is not only appointed by shareholders, but also reports to shareholders in the annual financial statements (see below). The fact that shareholders have to appoint the members of the audit committee on an annual basis highlights the important role 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 directors to nominate for appointment by the shareholders. Of course, the shareholders may appoint any director they deem fit and proper, as long as that director qualifies for appointment in terms of the ***Companies Act***.

Ethical leadership and social responsibility is highlighted in ***King IV***. These same sentiments are echoed in the ***Companies Act***. Although it may be argued that the provisions of the ***Companies Act*** with respect to the appointment of the audit committee 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 statements, internal financial controls, combined assurance, effective financial risk management, and meaningful integrated reporting to shareholders and stakeholders alike.

Section 94 of the ***Companies Act*** requires 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 three 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.

Appointment of the audit committee (continued)

The requirements of **Section 94** are prescriptive. Should the company appoint an audit committee with members other than those that meet the requirements for appointment in **Section 94**, it will 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 (including the process to nominate and appoint the external auditor), 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 (at least three), but each member must meet the criteria and must be a director of the company. In instances where an audit committee comprises more than three members, each of these members must meet the requirements for membership set out in the ***Companies Act*** – if one member does not meet the requirements, there would be an improperly constituted audit committee, and in effect no audit committee at all.

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. However, the audit committee may invite knowledgeable persons to attend its meetings, and may utilise advisors and obtain assistance from other persons inside and outside of the company.

As stated above, the ***JSE*** requires listed companies to appoint an audit committee in line with the requirements of the ***Companies Act***, and consider the practices of ***King IV*** on an apply or explain basis. In this regard it is important to note that ***King IV*** recommends that the chair of the board should not be a member of the audit committee.

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 ***King IV*** 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 IV require audit committee members to be independent

The question arises as to whether or not directors who are shareholders of the company (or even representatives of the shareholder) may be appointed to the audit committee. ***This question often arises where companies have a BEE partner.*** The ***Companies Act*** makes no reference to shareholding as a disqualification from membership of the audit committee, and the value judgement pertaining to independence relates only to suppliers and customers. The mere fact that a person holds shares in the company (or represents a shareholder) would not in itself preclude such a person from serving as a member of the audit committee. However, it is proposed that, in line with the best practice principles set out in ***King IV***, the appointment of shareholders or shareholder representatives to the audit committee should be carefully considered. A judgement on the effect of the shareholding or other relationships is required in order to establish the likely impact on the independence of a particular person. It should be noted that from a ***JSE*** perspective, any director that participates in a share incentive/option scheme, will not be regarded as independent.

For listed companies, the definition of independence as set out in ***King IV*** applies. The concept of independence has evolved from the position in ***King III***. Whereas ***King III*** provided a list of disqualifications from independence (i.e. where any of the listed disqualifications applied, a director is regarded as non-independent), ***King IV*** takes a more practical approach and rather focuses on the perception of independence. As such, factual independence or a tick-box approach is replaced by a much more balanced assessment of independence which requires consideration of substance over form. It is thus possible for someone that meets one or more of the ***(King III)*** disqualification criteria to nevertheless be regarded as independent. Although ***King IV*** rejects a tick-box approach for the independence assessment, it does provide a list of factors/criteria which may be considered during the independence inquiry. It is down to the Board to determine if a director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement. The yardstick for purposes of this assessment will be the perception of a reasonable and informed third party, i.e. whether or not an informed and reasonable outsider regards a director as independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement. The key question to be answered here is whether or not, a director has an interest, position, association or relationship which, when judged from the perspective of a reasonable and informed third party, is likely to influence unduly or cause bias in decision-making in the best interests of the company.

Independence of audit committee members (continued)

Where a company chooses to combine the audit and risk committee, membership of the committee should be carefully considered. Preferably, membership of the risk committee should include executive and non-executive directors. Given the difference in the membership of the risk and audit committee respectively, 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 the ***Companies Act*** and ***King IV***, i.e. the committee may only comprise independent non-executive directors.

Overview of the requirements relating to independence

Companies Act

Independent if:

- The director was not involved in the day-to-day management of the business for the previous financial year.
- The director was not a full-time employee or prescribed officer of the company or a related company during the previous three financial years.
- 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.
- The director is not related to anybody who falls within the above criteria.

King IV

The board should consider the following and other indicators holistically, and on a substance over form basis, when assessing the independence of a member of the governing body for purposes of categorisation:

The director:

- Is a significant provider of financial capital, or ongoing funding to the organisation; or is an officer, employee or a representative of such provider of financial capital or funding;
- If the organisation is a company, participates in a share-based incentive scheme offered by the company;
- If the organisation is a company, owns securities in the company the value of which is material to the personal wealth of the director;
- Has been in the employ of the organisation as an executive manager during the preceding three financial years, or is a related party to such executive manager;
- Has been the designated external auditor responsible for performing the statutory audit for the organisation, or a key member of the audit team of the external audit firm, during the preceding three financial years;
- Is a significant or ongoing professional adviser to the organisation, other than as a member of the governing body;
- Is a member of the governing body or the executive management of a significant customer of, or supplier to, the organisation;
- Is a member of the governing body or the executive management of another organisation which is a related party; or
- Is entitled to remuneration contingent on the performance of the organisation.

ACTION ITEM:
The board should always consider the independence of a director from the perspective of a reasonable and informed third party.

Qualifications and financial literacy

King IV requires that the audit committee should, as a collective, have the necessary skills and experience to meet its obligations. This should be considered by the nominations committee prior to the Annual General Meeting (AGM) when they nominate members for appointment to the audit committee. As a collective, the audit committee should have a good understanding of:

- Internal financial controls
- External audit process
- Internal audit process
- Corporate law
- Risk management
- Sustainability issues
- Integrated reporting, which includes financial reporting
- Governance of information and technology
- The general governance processes within the company

The **Companies Act Regulations Section 42** requires that at least one third of the members of the audit committee should have academic qualifications, or experience in economics, law, corporate governance, finance, accounting, commerce, industry, public affairs or human resource management.

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 judgement 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.

In order for the audit committee to function optimally, it is necessary for the members to be financially literate. Members of the audit committee should have a detailed understanding of financial reporting, which may include:

- An understanding of financial statements and international 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 issuer'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

Audit committee financial literacy recommendations	
1	Self-assessment should be thorough, not merely a compliance exercise, and should be repeated periodically
2	Members should understand auditing, accounting, and financial reporting issues relevant to the company and how management and the external auditor address them
3	Committees should anticipate and understand how pending financial reporting and regulatory developments may affect the company, and particularly its talent needs
4	Members should focus on committee composition, including independence, financial expertise, risk management, broad business or leadership experience, and succession planning

ACTION ITEM:
Audit committees should consider whether they have the necessary skills and expertise in these complex accounting and financial reporting areas.

Chair of audit committee

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

- The committee chair is demonstrably committed to the integrity of all aspects of corporate reporting (both in the annual report and on the company website), internal control, risk management and audit quality.
- The audit committee chair inspires confidence. The audit committee members value the chair's opinion and believe that the chair demonstrates clear leadership of the committee and acts as a driving force within the committee to ensure all audit committee members are contributing effectively.
- The audit committee chair brings an independent perspective and should challenge when it comes to management, the internal auditor and the external auditor.
- The audit committee chair performs their role with enthusiasm, acts as a catalyst for change and brings ideas and insights to help the organisation to be more successful.
- The audit committee chair has the confidence of shareholders and is proactive about seeking meetings with shareholders to seek input about significant matters within the remit of the committee.

Director qualification disclosure requirements

King IV proposes that the names, qualifications and experience of the members of the board of directors be disclosed. 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 serve on the company's board and/or audit committee.

Clear notes

Questions to consider: Composition

- 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?
- What process can the audit committee use to periodically assess its composition to confirm whether its members collectively have the skills and experience (e.g., financial acumen, industry, business, leadership) needed to fulfil the company's evolving needs and the committee's duties? Are gaps discussed with other board members, such as the nominating committee chair?
- How does the committee cultivate diversity of thought and composition to elicit multiple points of view that can help the committee effectively meet its responsibilities?
- What process can the committee consider for reconfirming the financial literacy of the audit committee members?
- What training and education programmes are available to help audit committee members maintain their financial knowledge and remain current with new developments and trends in areas included in the committee's oversight responsibilities, including company-specific needs or issues?
- How does the committee periodically assess, maintain, monitor, and review the independence of the audit committee members?

Additional notes

Section 3: Key responsibilities

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.

ACTION ITEM:
Develop an annual calendar that includes all meeting agendas, dates and times taking into account audit committee charter.

The committee should meet as many times as it considers necessary to meet its responsibilities under its terms of reference. Where the audit committee also has members or acts as a risk committee, further meetings may be required to ensure that adequate focus can be given to risk management and internal controls as well as the financial reporting cycle.

ACTION ITEM:
Action points for committees to consider are:

- Items on the agenda are set with consideration of regulatory requirements, the company's reporting timetable and after considering key issues identified by management, the chief risk officer, the director of internal audit and the external auditors; and, where applicable, the input sought from stakeholders such as shareholders or employees.
- The agenda gives appropriate focus on the most important issues, key judgements, and risk areas, ensuring that the committee's focus is spent on the most critical areas.
- The meeting cycle allows time for "deep dives" in areas of particular complexity or interest.

Meetings of the committee

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 dates when needed. Concurrent with the charter review, the committee should examine its calendar of company's 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 external auditor. When appropriate, the committee should also seek legal counsel in reviewing its charter and the calendar.

Tools and resources
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 IV***. The sample, which is reflected as **Appendix A**, may be used with the calendar planning tool in **Appendix B**.

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 IV***.

View a sample audit committee charter

View a sample calendar planning tool

Clear notes

Questions to consider: Charter

- How does the committee consider additional risks that have arisen related to committee responsibilities in the charter?
- What new responsibilities have been assigned or reassigned to the audit committee, and how have they been incorporated in the charter?
- How do committee members manage their time commitments to allow adequate attention to their responsibilities as outlined in the charter?
- How has the audit committee considered whether the responsibilities assigned to the committee are manageable? If the workload may hinder the committee's ability to execute its duties effectively, are there options for reallocating certain responsibilities to the board or other committees where reasonable?
- How does the committee align its activities with a calendar to incorporate both required activities as set forth in the charter and additional responsibilities of the audit committee as they emerge?
- What updates to the charter might the committee consider as a result of changes in the company?

Additional notes

Functions of the audit committee

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 and the auditor's terms of engagement
- 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
- 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.

Recommendation

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

To assist with this, and to encourage stakeholder alignment the concept should be introduced that companies should establish and publish an "Audit and Assurance Policy". This would make clearer the extent of all assurance activities, addressing the "audit universe" of internal and external audit as well as additional assurance activity often undertaken by specialists, over areas such as cyber risk or climate impacts.

Although currently there is no requirement for an audit committee to establish such a policy, it seems clear that this is a sensible codification of audit committee assurance considerations and therefore all audit committees should be encouraged to develop one, whether they choose to publish it or not. The rolling nature of the policy would make it simple to reflect changes in circumstances and to evidence learning.

ACTION ITEM:

The committee should address the following in its Audit and Assurance Policy:

- The audit committee considers the principal and emerging risks to the business and both its financial reporting and operational controls, and identifies any areas where additional audit or assurance coverage would be of benefit, for instance corporate culture, alternative performance measures, key performance indicators. The committee establishes a policy regarding which of these areas should be covered by internal or external auditors or other providers of assurance and how frequently that should happen.
- The audit committee determines its framework for decisions about materiality and is able to articulate this to stakeholders.
- The audit committee considers whether any form of assurance should be obtained over specific information conveyed in the annual report by the directors, in particular:
  - That the review of the company's business in the annual report is fair, balanced and comprehensive.
  - The confirmation that the annual report, as a whole, is "fair, balanced and understandable" and that it contains sufficient information to understand the position, performance, strategy and business model of the company.
  - The disclosures in the front half of the annual report regarding corporate purpose, whether it is clearly articulated and linked to the company's strategy and values, and the explanation of how purpose, strategy and values align with the company's culture.
  - Key performance indicators (KPIs), especially where KPIs and other metrics are of interest to investors and/or used to drive executive remuneration.
- The audit committee assesses whether there are significant corporate events or activities planned where assurance would provide benefits – such as changes in systems or control environment, new accounting judgements, acquisitions, new businesses being launched, outsourcing, planned divestments.
- The audit committee has considered the level of assurance over other information published by the company, such as:
  - Interim financial statements
  - Updates to the market
  - Presentations to analysts
  - Information provided to regulators
  - Sustainability reporting
- The audit committee considers whether input should be obtained from stakeholders such as shareholders or employees on its audit and assurance policy and if so puts in place procedures for this.

Functions of the audit committee (continued)

The Audit and Assurance Policy would:

- Explain what independent assurance, if any, the company intends to obtain in the next three years in relation to the annual report and other company disclosures beyond that required by statutory audit, including:
  - The company's sustainability reports in whole or part, and other disclosures related to risk; and
  - The effectiveness of the company's internal controls framework.
- A description of the company's internal auditing and assurance processes, including:
  - How management conclusions and judgements in the annual report and accounts can be challenged and verified internally; and
  - Whether, and if so how, the company is proposing to strengthen its internal audit and assurance capabilities over the next three years.
- A description of what policies the company may have in relation to the tendering of external audit services.
- An explanation of whether, and if so how, shareholder and employee views have been taken into account in the formulation of the Audit and Assurance Policy.
- Information on any assurance obtained over risk and viability reporting, and the effectiveness of a company's internal control framework.

In addition to the legislative duties set out above, ***King IV*** 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 risks relating to information and technology 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
- Satisfying itself with regard to the expertise, resources and experience of the finance function
- Oversight of the external audit process
- Disclosing its views on audit quality with reference to audit quality indicators.

Key item to consider is whether the audit committee assessed its confidence in the quality of the management information provided to it – from the finance function covering accounting and tax issues and judgements and, from other parts of the company, covering ethical and conduct matters, workforce information and compliance with laws and regulations. Where necessary the committee plans for additional assurance.

ACTION ITEM:
Additional assessment and possible discussion should be done with regard to internal audit and whether any changes were implemented by internal audit function that would affect the oversight of this function. Ensure audit committee has necessary knowledge of current affairs in relation to auditing specific changes that would have impacted the internal audit function and thus the oversight required.

Functions of the audit committee (continued)

The ***JSE Listings Requirements*** adds to this list in that it requires the audit committee to:

- Ensure that the issuer has established appropriate financial reporting procedures and that those procedures are operating, which should include consideration of all entities included in the consolidated group IFRS financial statements, to ensure that it has access to all the financial information of the issuer to allow the issuer to effectively prepare and report on the financial statements of the issuer
- Requesting relevant information from the auditors in order to assess the suitability for appointment of the audit firm and designated individual partner

What to request from the external auditor:

- The designated individual auditor's IRBA confirmation of registration to practise.
- The decision letter, findings report and proposed remedial actions to address the findings (if applicable), of the latest inspection the Independent Regulatory Board for Auditors (IRBA) performed on the audit firm. Redacted versions may be provided to protect the identities of entities mentioned in the documents.
- The designated individual auditor's quality history information. This should include external inspections, such as inspection by the IRBA or foreign audit regulators, as well as internal inspections conducted by the audit firm's monitoring teams. Ideally, the quality history should be as comprehensive as possible, but should include information for at least five years so as to provide the audit committee with a holistic view of the individual auditor's quality history.

Audit Quality Indicators (AQI's) to consider can be found on the IRBA's website.

Since the ***Companies Act*** prescribes the appointment process, composition and functions of the audit committee, it can 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. In instances where a company fails to appoint an audit committee where the ***Companies Act*** requires such appointment, or the composition of the committee does not comply with the requirements of the ***Companies Act*** (i.e. there is no statutory audit committee), the board of the company may be able to perform some of the functions of the audit committee as set out above. However, the ***Companies Act*** poses restrictions as to which duties the board may perform. **Section 94(10)** restricts the board from taking on the duties of the audit committee relating to auditor appointment, fees and terms of engagement of the auditor.

ACTION ITEM:
The audit committee should review this information together with Audit Quality Indicators (AQIs) to ensure a holistic understanding of the individual auditor and audit firm's quality.

Non-audit services

The ***Companies Act*** requires that the audit committee determines the nature and extent of non-audit services, and that the committee pre-approves any agreement for the provision of non-audit services by the auditor. In order to determine what constitutes "non-audit services" it is necessary to be clear on the services that will be performed by the auditor as part of the audit.

It is proposed that the auditor engages with the audit committee on a regular basis and tables for approval the extent of fees to be paid or paid in respect of proposed/requested non-audit services. Any agreement for the provision of non-audit services 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 should be pre-approved by the audit committee.

A number of important changes were recently made to the International Ethics Standards Board for Accountant's (IESBA) Code of Ethics for Professional Accountants (the Code). The new provisions promote greater public transparency and establish base level requirements for communication between auditors and those charged with governance. In particular, the revisions to the Code are aimed at addressing potential threats to independence.

The Code introduces stricter rules on the provision of non-audit services to audit clients classified as Public Interest Entities (PIEs). The Code defines PIEs as publicly traded entities, deposit taking entities such as banks, insurers, and entities classified as PIEs in terms of local laws and regulatory requirements.

Recent revisions to PIE definition

The new and much stricter prohibitions introduced relate to the audit firm:

- Providing non-audit services to a PIE audit client if it might create a self-review threat (in other words, the threat that the audit firm will be auditing its own work);
- Representing a PIE audit client before a tribunal or court;
- Acting as an expert witness (there are certain exceptions provided for in the Code);
- Advising on taxation matters where a significant purpose is tax avoidance, and taxation treatment is not likely to prevail under taxation law or regulation;
- Advising on investing in the client's securities; and
- Recruiting and/or advising on the terms of employment of officers, directors, and senior management.

Furthermore, the Code requires enhanced disclosure from management of fees paid to the auditor to increase transparency and benefit stakeholders.

The revisions apply to audits of financial statements beginning on or after 15 December 2022. Services contracted and in progress before 15 December 2022 can be completed under non-audit services rules as they existed prior to above amendments.

Non-audit services may create threats to independence and is thus an important area for the audit committee to thoroughly evaluate. The audit committee should ensure that these non-audit services can be provided to the entity as assurance or audit clients, as well as taking into account any affiliates and their respective services.

Reporting and disclosure

The audit committee is obliged in line with the ***Companies Act*** to report to shareholders by including in the annual financial statements (AFS) 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.

King IV proposes that the audit committee makes a number of disclosures in addition to the disclosures required in terms of the ***Companies Act***. The intention is to demonstrate accountability and transparency and provide stakeholders with a level of comfort that the audit committee fulfils its function diligently.

It is proposed in ***King IV*** that the audit committee include the following information in the audit committee report:

- A summary of the role of the audit committee
- An indication that all the members of the committee comply with the statutory requirements as per the ***Companies Act***, as well as the names and qualifications of all members of the audit committee during the period
- The number of audit committee meetings, and the record of attendance of the different members
- An overview of the results of the audit committee's performance evaluation
- A statement as to whether the audit committee is satisfied that the external auditor is independent of the organisation. The statement should specifically address:
  - The policy and controls that address the provision of non-audit services by the external auditor, and the nature and extent of such services rendered during the financial year
  - The tenure of the external audit firm and, in the event of the firm having been involved in a merger or acquisition, including the tenure of the predecessor firm
  - The rotation of the designated external audit partner
- The audit committee's views on the quality of the external audit, with reference to audit quality indicators (AQIs) such as those that may be included in inspection reports issued by external audit regulators. An explanation of how the committee has assessed the effectiveness of the external audit process and the approach taken for the appointment or reappointment of the external auditor; the length of tenure of the current audit firm; the current audit partner name, and for how long the partner has held the role
- If the external auditor provides non-audit services, the committee's policy for approval of non-audit services; how auditor objectivity and independence is safeguarded; consideration to the threats created by each service individually and whether the combined effect of such services creates or impacts threats to independence; the audit fees for the statutory audit of the company's consolidated financial statements paid to the auditor and its network firms for audit related services and other non-audit services, including the ratio of audit to non-audit work; and for each significant engagement, or category of engagements, explain what the services are and why the audit committee concluded that it was in the interests of the company to purchase them from the external auditor
- Significant changes in the management of the organisation during the external audit firm's tenure which may mitigate the risk of familiarity between the external auditor and management
- Significant matters that the audit committee has considered in relation to the annual financial statements, and how these were addressed by the committee, having regard to matters communicated to it by the auditors. The committee needs to exercise judgement in deciding which of the issues it considered in relation to the financial statements were significant. The audit committee should aim to describe the significant issues in a concise and understandable form while reporting on the specific circumstances of the company. When reporting on the significant issues, the audit committee would not be expected to disclose information which, in its opinion, would be prejudicial to the interests of the company (for example, because it related to impending developments or matters in the course of negotiation)
- The audit committee's views on the effectiveness of the chief audit executive and the arrangements for internal audit. Including an explanation of how the committee has assessed the effectiveness of internal audit and satisfied itself that the quality, experience and expertise of the function is appropriate for the business
- The audit committee's views on the effectiveness of the design and implementation of internal financial controls, and on the nature and extent of any significant weaknesses in the design, implementation or execution of internal financial controls that resulted in material financial loss, fraud, corruption or error
- The audit committee's views on the effectiveness of the CFO (this is also required in terms of the ***JSE Listings Requirements***) and the finance function
- The arrangements in place for combined assurance and the committee's views on its effectiveness.

ACTION ITEM:
Committee to consider all aspects of non-audit services including:

- Policy for approval
- Safeguards to objectivity and independence
- Audit fees for statutory audit of consolidated financial statements
- Network firms of consolidated entity's fees relating to audit and non-audit services
- Ratio of audit to non-audit services
- Explanation for each significant category of service and why it was required to purchase

Reporting and disclosure in terms of the IESBA Code

If an audit client meets the definition of a Public Interest Entity (PIE), stakeholders have heightened expectations regarding the auditor's independence. The IESBA Code requires the audit firm to communicate fee-related information about both audit and non-audit services with those charged with governance of PIE audit clients. The audit firm needs to disclose fees paid or payable to the firm or network firms for the audit of the financial statements on which the firm expresses an opinion, and whether threats created by the level of the fees are at an acceptable level; and if not, any actions the firm has taken or will take to ensure that the threat is at an acceptable level. The firm must also communicate fees for non-audit services charged to the PIE audit client during the period covered by the financial statements on which the firm expresses an opinion.

ACTION ITEM:
Independence is an important element to consider. If a threat to independence has been identified, the firm must indicate whether the threats are at an acceptable level, and if not, what it proposes to do to ensure that threats are reduced to an acceptable level.

If the total fees a firm generates from expressing the audit opinion represents a large proportion of the total fees of that firm, the dependence on that client and concern about potentially losing the client create threats to the firm's independence. To this end, where an audit client is a PIE and, for two consecutive years, the total fees from the client and its related entities represent more than 15% of the total fees received by the firm expressing the opinion on the client's financial statements, the audit firm needs to disclose this dependency to those charged with governance of the audit client, as well as the safeguards applied to address the threats created. Note that the threshold for non-PIE audit clients is a fee dependency of 30% of the total fees received by the firm.

The IESBA Code also encourages public disclosure of the fee-related information above. If local laws and regulations do not require the audit client to disclose such fee-related information, the audit firm should discuss with those charged with governance the benefit that such disclosure will have in that it will enhance the stakeholders understanding of fees paid and their impact on the audit firm's independence.

Those charged with governance should consider public disclosure of:

- Comparative information of the prior year's fees for audit and non-audit services;
- Nature of the services provided and their associated fees; and
- Safeguards applied when the total fees from the client represent or are likely to represent more than 15% of the total fees received by the firm.

To the extent that those charged with governance of the PIE audit client decides not to publicly disclose the above-mentioned (see information), the information will be disclosed by the audit firm in, for example, the auditor's report or transparency report.

For listed companies, the audit committee must report to shareholders in the annual report that it:

- Considered, on an annual basis, and satisfied itself of the appropriateness of the expertise and experience of the financial director
- Ensured that the company established appropriate financial reporting procedures, and that those procedures are operating
- Request from the audit firm relevant information for their assessment of the suitability for appointment of the designated individual partner both when they are appointed for the first time and thereafter annually for every reappointment
- A brief description of the committee mandates, the number of meetings held and other relevant information as required by ***JSE Listing Requirements***.

There is no requirement for the full audit committee report to be included in the annual financial statements. Most companies prepare a report on the statutory requirements for inclusion in the annual financial statements, and then prepare a more comprehensive report for inclusion in the integrated annual report.

Relationship with the board

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

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

ACTION ITEM:
The audit committee should ensure they discuss what information and assurance it requires in order to properly carry out its role to review, monitor and provide assurance or recommendations to the board and, where there are gaps, how these should be addressed. The audit committee satisfies itself that these sources of assurance and information are sufficient and objective.

Clear notes

Questions to consider: Audit committee reporting

- How effectively does the audit committee's report describe for investors and other stakeholders the audit committee's oversight responsibilities?
- How has the role of the audit committee evolved to include areas such as cyber, ESG, enterprise risk management, or others, and how are these changes being disclosed to stakeholders in the Audit Committee's Report?
- To what extent are the qualifications, experiences, and diversity considerations of audit committee members disclosed?
- How does the audit committee describe in the company's proxy statement the committee's oversight of and engagement with the independent auditor?
- To what extent does disclosure address issues such as auditor independence, auditor performance, and other matters of interest to investors?
- How has the disclosure of audit and non-audit services been considered in the audit committee report?
- Has the committee considered the PIE definition and additional disclosures possibly required if the company is seen as a PIE?
- Has all the disclosure of the JSE Listing Requirements been included in the audit committee report?

Additional notes

Appointment of the external auditor

Over the last few years the ***IRBA*** has requested information related to Audit Quality Indicators (AQIs) for audits of PIEs specifically from JSE-accredited audit firms. These AQIs can assist the audit committee when appointing an external auditor and when considering the individual designated auditor. The AQIs are useful in the tendering process, especially when comparing audit firms. The following AQIs are particularly relevant:

- The experience of the individual designated auditor as an engagement partner. The greater the number of years, the more experienced the partner is likely to be. The audit committee could enquire whether the individual designated auditor has complied with all Continuing Professional Development (CPD) requirements.
- Workload of the engagement partner role (%). This AQI is a measure of the engagement partner hours charged to the audit client as a percentage of total audit hours charged to the audit client for completed engagements. It provides an indication of the audit partner's level of involvement in the engagement. Higher ratios indicate greater involvement of the individual designated engagement partner and may be indicative of a higher quality audit file, or an audit with more areas of significant judgment. Alternatively, high ratios may indicate an understaffed or inexperienced engagement team, or other execution issues. This ratio can be compared to the engagement quality control review (EQCR) partner hours (%) ratio for example.
- Technical resources: partner ratio. This AQI entails the engagement partner to technical partner ratio. The higher the ratio, the more engagement partners a technical partner serves. Accordingly, a high ratio may indicate that an engagement partner does not have as much access to a technical partner resource compared to an engagement partner in a firm with a lower ratio. The nature of the firm, as well as the nature and scope of the engagement is key to understand this ratio.
- Other AQIs the audit committee can consider: staff turnover, training (hours per person), workload: manager supervision (%), partner coverage (%) etc.

Note: AQIs must always be interpreted in light of the context.

The audit committee should consider and possibly request the following from the external auditor in line with the ***JSE Listings Requirements***:

- Consider, on an annual basis, and satisfy itself of the appropriateness of the expertise and experience of the financial director;
- Ensure that the issuer has established appropriate financial reporting procedures and that those procedures are operating, which should include consideration of all entities included in the consolidated group IFRS financial statements, to ensure that it has access to all the financial information of the issuer to allow the issuer to effectively prepare and report on the financial statements of the issuer;
- Consider in the assessment of suitability of the appointment of the auditor:
  - The latest results (including related remedial action plan) of all inspections performed by its regulator. The audit committee may accept reports with the identity of specific entities redacted provided that such redaction does not limit the understanding of their content;
  - Any new inspection result of an inspection performed by its regulator, between the date of appointment of the auditor and the date of signature of the audit report on the annual financial statements;
  - A summary, by the auditor, of the ongoing communication related to monitoring and remediation referred to in paragraph 46 of International Standard on Quality Management 1 (ISQM 1); and
  - A summary of any legal or disciplinary proceedings completed or pending, as determined by the head of risk or a person with similar authority within the past seven years. Legal or disciplinary proceedings include those instituted through any legislation or by any regulatory/professional body; and
- Notwithstanding the provisions of **Section 90(6)** of the ***Companies Act***, ensure that the appointment of the auditor is presented and included as a resolution at the annual general meeting of the issuer pursuant to **Section 61(8)** of the ***Companies Act***.

The above will be confirmed by the issuer by reporting to shareholders in its annual report, that the audit committee has executed the responsibilities set out in 3.84(g) and is thus important for consideration by the audit committee.

The audit committee should ensure that the listed company has a process in place to notify the JSE of a change in its external auditor, whether as a result of termination of appointment or resignation, and a change in the individual designated auditor. This must be done as soon as possible, but no later than two business days following the decision to terminate an external auditor's appointment, or receiving notice of the external auditor's resignation.

Appointment of the external auditor (continued)

The audit committee is a critical part of the auditor appointment process. In terms of **Section 94** of the ***Companies Act***, the audit committee's duties include nominating an auditor for appointment that in their opinion is independent. Where the shareholders appoint an auditor other than the auditor nominated by the audit committee, the audit committee must be satisfied with the independence of the appointed auditor. Accordingly, where the independence of the auditor has not been ratified by a properly constituted audit committee (e.g. less than three members, or not every member of the committee is an independent non-executive director), the auditor's appointment is invalid.

Where a firm is appointed as auditor, the audit committee must also verify the independence of the individual that will be responsible for the audit (the designated auditor). The name of the designated auditor must be included in the Register of Auditors as contemplated in **Section 85** of the ***Companies Act***.

Where the independence of the auditor has not been ratified by a properly constituted audit committee there is a risk that if an audit committee is subsequently formed (either at the instance of the company or because the ***Companies and Intellectual Property Commission (CIPC)*** issues a compliance notice in terms of **Section 84(6)** of the ***Companies Act***) and that audit committee is not satisfied with the auditor's independence, the auditor's appointment will accordingly not be ratified and will thus be invalid.

ACTION ITEM:
Consider whether audit committee is properly constituted as per Section 94 of the ***Companies Act*** and whether the appointment of an external auditor is regarded as valid and appropriate.

For listed companies, the audit committee must request relevant information from the auditors (including the last inspection findings of the ***Independent Regulatory Board for Auditors (IRBA)***) in order to assess the suitability for appointment of the audit firm and designated individual partner.

Section 90(6) of the ***Companies Act*** provides that a retiring auditor may be automatically reappointed at an AGM without any resolution being passed, unless:

- The retiring auditor is no longer qualified for appointment, no longer willing to accept the appointment, and has so notified the company, or is required to rotate off as auditor as provided for in **Section 92**;
- An audit committee appointed by the company in terms of ***the Companies Act*** objects to the reappointment; or
- The company has notice of an intended resolution to appoint some other person or people in place of the retiring auditor.

It is advisable that, despite the ***Companies Act's*** allowing for the automatic reappointment of the auditor without passing a resolution, the company pass a resolution due to the appointment of the auditor being an annual appointment required.

Once the shareholders have appointed the external auditor, an engagement letter should be signed between the audit firm and the company. The engagement letter should identify the audit firm and the individual auditor. Even though the ***Companies Act*** determines that the audit committee bears exclusive responsibility for the appointment and terms of engagements of the external auditor, there is no statutory requirement for a member of the committee to sign the engagement letter on behalf of the company.

Assessment of the independence of the external auditor

The ***Companies Act*** and ***King IV*** 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.

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 are set out. Both the person responsible for the audit as well as the audit firm are prohibited from providing accounting, bookkeeping 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 or audit firm will be disqualified from appointment. As such, the audit committee needs to request the auditor and management to provide detail with respect to the non-audit services provided by the auditor prior to appointment, and specifically consider whether or not the auditor (or any other member of the audit firm) provided any of the prohibited services (bookkeeping, accounting, related secretarial services, maintenance of financial records or preparation of the financial statements) to the company in the preceding five years.

Useful tips when considering auditor independence

To assess the independence, the audit committee can consider an AQI such as independence: non-audit fees %. This AQI entails non-audit fees billed (amount invoiced) to the audit client as a percentage of the total audit fees billed (amount invoiced) to the audit client for completed audit engagements and is presented as an average per firm. This measure will assist the audit committee to detect potential threats to the auditor's independence. The higher the percentage, the more fees the auditor receives for non-audit services.

A firm's tenure is an indicator of independence or a familiarity threat. A familiarity threat entails that where there is a long standing relationship between the external auditor and the client, the auditor could become too sympathetic to the client's interests, and not critical enough of their work. Generally, the longer the tenure, the greater the risk of a familiarity threat which ultimately impairs independence.

IRBA introduced a mandatory audit firm rotation (MAFR) rule. MAFR applies to auditors of all Public Interest Entities (PIEs) as defined in **Section 290.25 to 290.26 of the amended IRBA Code of Professional Conduct for Registered Auditors**. The requirement is effective for financial years beginning on or after 1 April 2023.

In terms of MAFR the audit firm may not accept the appointment as auditor of the firm, if served as the auditor of the PIE for more than 10 consecutive financial years. The audit firm can only become eligible for reappointment after a cooling off period of five years. When the auditor establishes that an audit client becomes a PIE, the period of time the auditor served the PIE as auditor before the client became a PIE will be included when determining the rotation timing.

IRBA provided transitional provisions in relation to joint auditors. If, at the effective date, the PIE is audited by joint auditors and both have exceeded the 10-year audit tenure, only one firm is required to rotate at the effective date and the remaining audit firm will have an additional two years before being required to rotate. This provision will only be applicable upon the effective date.

At the time of publishing the MAFR rule has been set aside by Supreme Court of Appeal.

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.

King IV recommends that the audit committee should confirm and oversee the independence of the external auditor, and consider the following:

- The provision of non-audit services by the external auditor, and the nature and extent of such services rendered during the financial year
- The tenure of the external audit firm
- Rotation of the designated external audit partner
- Any significant changes in the management of the organisation during the external audit firm's tenure which may mitigate the attendant risk of familiarity between the external auditor and management.

Of course, the audit committee should also consider the quality of the external audit.

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 and potential disqualification in terms of **Section 90(2)** of the ***Companies Act*** 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, ensure that the service will not be provided by a member of the audit team
- Partners of the audit firm, 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

Assessment of the independence of the external auditor (continued)

Overview of the requirements relating to independence

Section 94(7) of the Companies Act
Audit committee's statutory duties to ensure the independence of the external auditor

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 94, 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 pre-approve 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
    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
    iv. Any related matter
    v. To make submissions to the board on any matter concerning the company's accounting policies, financial control, records and reporting; and
    vi. To perform such other oversight functions as may be determined by the board

Section 94(8) of the Companies Act
Assessment of independence

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; and
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.

Assessment of the finance function

King IV 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.

Clear notes

Questions to consider: Evaluation of 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?
- Are 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 whistleblowing 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 towards a sound internal control environment?
- 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?

Additional notes

Interaction with management

Management has to ensure the audit committee is kept properly informed, and should take the initiative in supplying information rather than waiting to be asked. The audit committee needs to cultivate a transparent and constructive relationship with management, 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 regulations; as well as matters relating to accounting policies and judgements and the internal controls over financial reporting (ICFR), are heavily dependent on how open the relationship between management and the audit committee is. Disagreements between management and the audit committee are a potential signal of significant deficiencies in internal control, higher risk of errors in the financial reporting process and increased fraud risks.

Oversight of internal financial controls

King IV proposes that the audit committee provides disclosure on the committee's views on the effectiveness of the design and implementation of internal financial controls, and on the nature and extent of any significant weaknesses in the design, implementation or execution of internal financial controls that resulted in material financial loss, fraud, corruption or error.

More often than not, the board will delegate to the audit committee the responsibility for the company's internal control systems as well as management of the financial risks. The audit committee should review the company's internal financial controls, and should consider what role it can play in promoting sound risk management and internal control systems, including operational and compliance controls, and review these systems regularly. Management should provide the audit committee with reports on the effectiveness of the systems they have established and the results of any testing carried out by internal or external auditors. It is advisable for the audit committee to consider the level of assurance it is getting on the risk management and internal control systems, including internal financial controls.

The JSE requires, as per paragraph 3.84 (k) of the Listings Requirements, sign-off by the CEO and CFO on a prescribed statement on the effectiveness of financial controls.

ACTION ITEM:
The audit committee should ensure this statement has been provided and signed as required and also consider whether further evaluation of these internal financial controls are needed. The audit committee should also ensure the statement is supported with the necessary evidence.

Further evaluation can require either a detailed assessment or a high-level maturity assessment. A recommendation of applicable controls framework could be Committee of Sponsoring Organizations (COSO) structures, processes and systems in line with their five key control areas listed below:

- Control environment
- Risk assessment
- Control activities
- Information and communication
- Monitoring activities

View Committee of Sponsoring Organizations of the Treadway Commission – Home (coso.org)

Clear notes

Questions to consider: Internal control over financial reporting

- What is the committee's level of understanding with respect to key risks and related controls identified by management, the independent auditor, and internal audit?
- To what extent does the company rely on third-party service providers, and how are controls and processes over these relationships and data flows managed?
- Have there been any changes in the design and monitoring of controls? How has management ensured that controls have been appropriately redesigned?
- What new internal controls should be considered if there are shifts in the business operating model, such as a shift to remote or hybrid work?
- How well resourced is the company to adequately perform internal control activities? Has the company engaged specialists, where applicable, in evaluating controls over complex or IT-dependent processes?
- Has management defined and implemented remediation plans for deficiencies? If those remediation plans span a specific time frame, have temporary compensating controls been implemented to mitigate risk? How is management held accountable for timely remediation?

Additional notes

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 external auditor.

In support of these objectives, audit committees should take steps to facilitate a mutually beneficial relationship with the internal auditors:

- Meet privately with the internal auditors on a regular basis
- Encourage open communication between the chief audit executive (CAE) and the audit committee
- Take responsibility for the appointment, performance assessment and dismissal of the CAE or outsourced internal audit function
- Set clear goals and evaluate the performance of the CAE (these responsibilities should not be delegated solely to the CFO or CEO)
- 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 the CAE reports potential management lapses.

ACTION ITEM:
The internal audit plan should be presented and approved by the audit committee

Interaction with the internal auditors (continued)

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

01. The audit committee engages in an open, transparent relationship with the CAE.
02. The audit committee reviews and approves the internal audit charter annually.
03. The audit committee has a clear understanding of the strengths and weaknesses of the organisation's internal control and risk management systems.
04. The approved plan is carried out by competent, objective professionals from internal audit.
05. Internal audit is empowered to be independent by its appropriate reporting relationship.
06. The audit committee addresses with the CAE all issues related to independence and objectivity.
07. Internal audit is quality oriented and has a robust quality improvement programme.
08. The audit committee regularly communicates with the CAE about performance and improvement opportunities.
09. Internal audit reports are actionable and recommendations are implemented.
10. The audit committee meets periodically with the CAE without management.

Internal audit oversight

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.

Audit committees are generally responsible for financial risks and for overseeing the process for identifying and addressing those risks. 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.

ACTION ITEM:
The audit committee should focus on areas of major financial risk exposure and discuss with management the guidelines and policies for addressing these areas appropriately.

Consequently, risk oversight has been on the agenda of audit committees for a number of years. ***King IV*** 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 and other risks that may affect the integrity of the company's external reports (e.g. financial reporting risks, internal financial controls, fraud risk as it relates to financial reporting, and risks pertaining to information and technology).

Clear notes

Questions to consider: Internal audit

- 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?
- How flexible and dynamic is internal audit in addressing new risks promptly and meeting the needs of the audit committee? How does the mix of experience and capabilities in the internal audit team – for example, in areas such as technology and emerging risks – meet the current needs of the company?
- 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 external 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 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?
- How effective is internal audit in using advanced technologies, such as data analytics, to improve audit quality?
- How does the internal audit function comply with the International Standards for the Professional Practice of Internal Auditing as issued by the Institute of Internal Auditors?
- To what extent does the internal audit function have and demonstrate the level of independence needed to execute its responsibilities properly? How does internal audit's reporting structure within the company support independence and enable internal audit to perform effectively?

Additional notes

Clear notes

Questions to consider: Enterprise Risk Management (ERM)

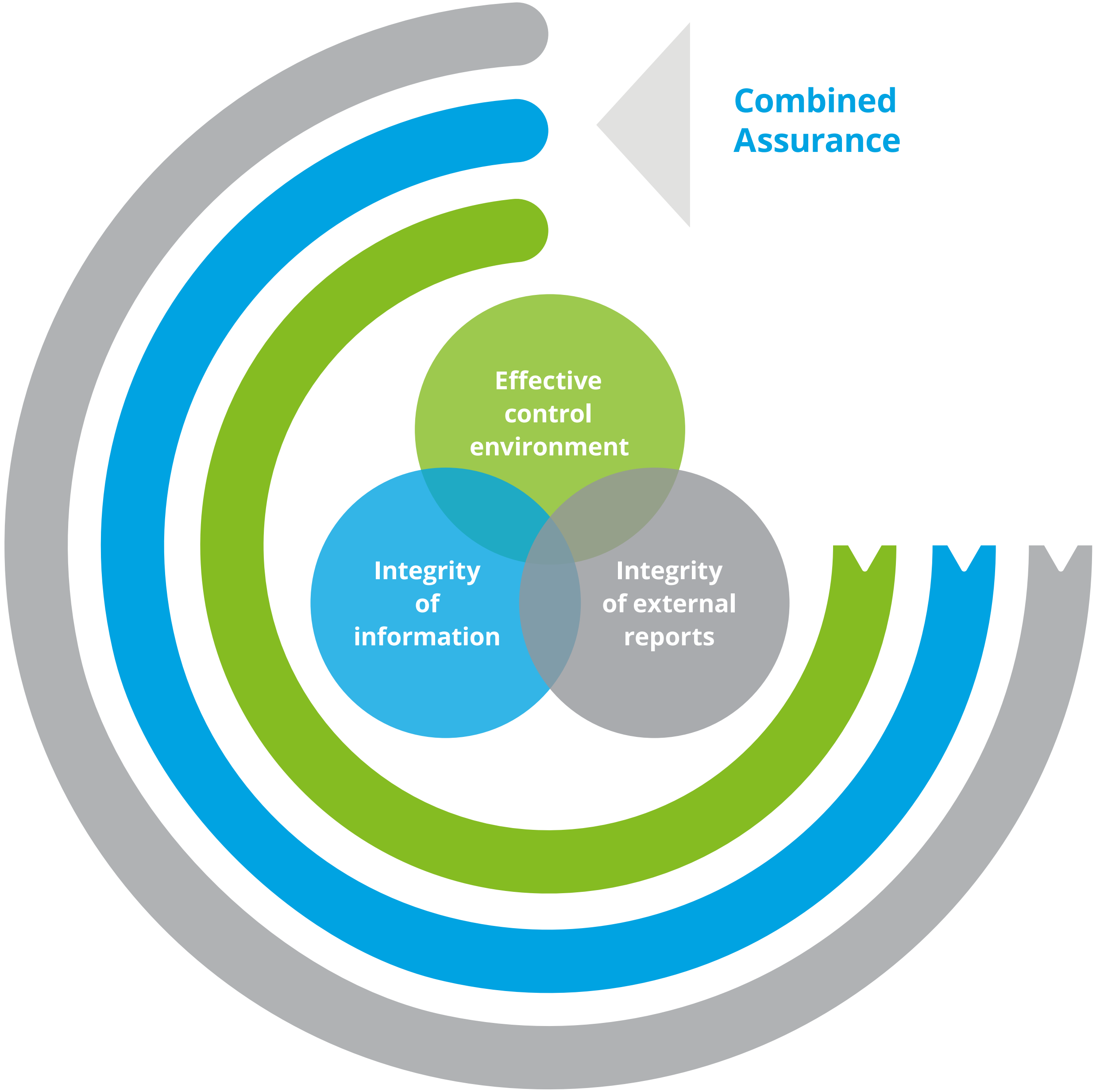
- To what extent does the board and its committees agree on where primary responsibility lies for overseeing the ERM programme and related processes?
- How clearly are oversight responsibilities for key risks delegated to the board and individual committees? How frequently is this delineation of responsibilities reassessed? How clearly is responsibility for key risks assigned to management, and does each risk have a member of management noted as the risk owner?
- How often is ERM on the audit committee's agenda, if appropriate, and what information is being provided in support of this? How does the audit committee confirm that new or emerging risks are considered and that board oversight responsibility is clearly defined?
- How does internal audit's plan align with the key risks identified in the ERM programme?
- How are management and internal audit staying ahead of emerging and evolving risk areas such as technology, cyber, and ESG?
- How is management considering unlikely but potentially severe risks that could have a significant detrimental effect on the organisation?
- How are risks to the extended enterprise, including third-party risks, assessed?

Additional notes

Combined assurance

King IV positions combined assurance as a core component of corporate governance. Combined assurance can be explained as the assessment by the various assurance providers of the level of risk mitigation and assurance being provided over risk, control, information and reports.

King IV defines the combined assurance model as the "model [that] incorporates and optimises all assurance services and functions so that, taken as a whole, these enable an effective control environment; support the integrity of information used for internal decision making by management, the governing body and its committees, and; support the integrity of the company's external reports".



The principles that guide combined assurance have been detailed as follows:

1. Primary responsibility for management of risk and control rests with management

2. Management considers and implements appropriate risk responses (within risk appetite)

3. Continuous monitoring of risk and control by management, supported by Risk Managers

4. Management is responsible for remediation of control deficiencies (corrective action), management of issues, and standards of performance

5. Internal control deficiencies should be reported to responsible parties, Senior Management and the Board

6. Common definition of the control environment and documentation of risks and controls should be in place

7. Common application of the approved risk taxonomy (defining and categorising risk and appropriate risk responses)

8. Risk-based response to providing assurance over risks and controls

9. Assurance over Internal Financial Controls (IFC's), information and reporting are incorporated

10. Continual co-ordination and engagement between assurance providers, while understanding the various mandates

11. Annual written assessment by Combined Assurance Model (CAM) owner to support the effectiveness assessment of the audit committee

The combined assurance model and process should be supported by a formalised policy and framework. The board and audit committee should approve the policy to ensure that the necessary oversight of and alignment with the combined assurance process is in place.

King IV proposes that the board assumes responsibility for assurance by setting the direction concerning the arrangements for assurance services and functions, and should delegate this function to the audit committee. In order to set this direction, management should present the policy and framework to the board and audit committee for approval.

The formalisation of the policy and framework enables key design principles to be refined for a particular company. These design principles include:

- Defining the levels of assurance
- Defining the assurance providers
- Defining the assessment criteria used to assess the quality of assurance
- Articulating the mandate of the combined assurance forum
- Defining the evidence required to support the assurance provider

The combined assurance process is supported by policy and models that can be implemented to provide a view on the effectiveness of the implementation of combined assurance.

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 anti-fraud 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, inappropriate use of shell companies, bribes to influence decision-makers, tender irregularities 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 (ICFR). 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 external auditor to gain the knowledge needed to provide appropriate oversight.

Leading practices for the oversight of financial reporting and internal controls

- Understand key controls and reporting risk areas as assessed by management, the internal auditors, and the external auditor
- Emphasise oversight of corporate taxes, an area where high-risk 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 judgements 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.

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 audit committee should also have an awareness of industry specific Acts and Regulations that might be applicable to the company.

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.

Clear notes

Questions to consider: Financial reporting

- How have changes in the business impacted accounting and disclosures, including estimates and judgments?
- Where management has accounted for an estimate from a range of possibilities, why did management select the point in the range? If management selected another point in the range, how would that impact the financial statements?
- Did the company record all known misstatements? If not, how did management consider materiality, as well as the control impact, of the misstatements?
- If the company includes forward-looking statements, how confident is management in its ability to forecast earnings accurately? Is the disclosure of a range of earnings estimates preferable to a specific target, and has management considered seeking input directly from shareholders regarding the types of forward-looking information they would find meaningful?
- What disclosure controls and procedures are in place related to the disclosure of non-GAAP measures?
- Is the non-GAAP measure prepared consistently from period to period in accordance with a defined policy, and is it comparable to that of the company's peers? Is the measure balanced? For example, does it adjust not only for non-recurring expenses but also for non-recurring gains?
- How clear is the audit committee's understanding of how non-GAAP measures impact compensation? To what extent are the audit and remuneration committees aligned on this?

Additional notes

Clear notes

Questions to consider: Fraud

- At what levels within the organisation are fraud risk assessments performed? For example, are assessments performed at the entity level, at significant locations or business units, on significant account balance, or at the major process level?
- How do management and the board consider the risk of management override of controls?
- How has management considered the potential for emerging fraud risks, and what has been the process for developing and assessing the appropriate internal controls?
- How have shifts in the organisation's talent model and the associated job responsibilities affected whether there is an appropriate segregation of duties?
- How does the company map or link identified fraud risks to control activities designed to mitigate the fraud risks?
- To what extent has management designed and implemented preventative controls to stop fraud from occurring as well as detective controls to identify the fraud if it occurs?

Additional notes

Complaint hotline procedures

Companies use hotlines to report a range of potential 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 the necessary 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 ensure 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 should also be provided with an ongoing 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 the following:

- 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 the company's web site, email, 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 whistleblower 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.

Clear notes

Questions to consider: Hotlines

- Does the committee understand how hotlines are evaluated, tested, and audited? To what extent do hotline processes and controls confirm that calls are received, recorded, and managed in a consistent, confidential, accurate, and timely manner?
- Has the hotline and whistleblowing process been evaluated and benchmarked by an independent third-party expert or consultant?
- Has the audit committee, directly or through the internal audit function, made an anonymous report to the whistleblower system alleging financial reporting fraud or other wrongdoing by senior management, to test the integrity of the flow of communications directly to the audit committee without management intervention?
- Does the level of alleged or suspected fraud and other violations of organisation policies reported through the whistleblower system or other channels suggest that the tone at the top or the tone communicated by management may need strengthening?
- Are there regular company-wide trainings and communications in place for employees to learn about code of ethics, hotlines, and whistleblower functions?

Additional notes

Clear notes

Questions to consider: Code of ethics/conduct

- How does the reporting process keep the audit committee informed of ethics and compliance issues as well as the actions taken to address them? How regularly does the committee discuss ethics and compliance?
- How frequently does the committee hear directly from the person who has day-to-day responsibility for ethics and compliance matters? To what extent does the committee consider holding these discussions in an executive session?
- How systematically does the company scrutinise the sources of ethics and compliance failures and respond to them?
- How does management act on reports? What evidence is captured regarding prompt, appropriate, and consistent disciplinary measures?
- How does the audit committee engage external advisers to conduct independent investigations?
- What ongoing monitoring and auditing processes are in place to assess the effectiveness of the ethics and compliance programme?

Additional notes

Section 4: Interaction with the external auditor

Section 4: Interaction with the external auditor

The audit committee is a critical part of the process to appoint the external auditor. In terms of **Section 94** of the ***Companies Act***, the audit committee's duties include nominating an auditor for appointment that in their opinion is independent. Where the shareholders appoint an auditor other than the auditor nominated by the audit committee, the audit committee must be satisfied with the independence of the appointed auditor. Accordingly, where the independence of the auditor has not been ratified by a properly constituted audit committee, the auditor's appointment may be invalid.

Audit committees of companies are responsible for the appointment, compensation, and oversight of the external auditor, including the resolution of any disagreements with management. It is paramount that the audit committee, management, the internal auditors, and the external 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 external auditor include

- Exercise ownership of the relationship with the external 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, valuations)
- 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 external auditor
- Focus on independence, including a process for the pre-approval of services beyond the audit (non-audit services)
- Provide formal evaluations and regular feedback

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

The audit committee should have a process for overseeing management's resolution of significant issues raised by the external auditor.

Clear notes

Questions to consider: Oversight of the independent auditor (external auditor)

- Does the independent auditor have sufficient knowledge and experience to address the risks and types of transactions managed by the company, and are the auditor's specialists engaged where applicable?
- Does the independent auditor communicate to the committee in a clear, succinct, and timely manner? Is communication focused and prioritised on the right areas?
- Is the committee engaging in an ongoing dialogue, both formal and informal, with the independent auditor to discuss topics beyond required communications? Does dialogue include, for example, perspectives on management and tone at the top, business trends, and the regulatory environment in financial reporting and standard setting?
- In instances where the company's needs are evolving, is the independent auditor also evolving with appropriate talent to serve the company?
- How does the independent auditor evaluate the reasonableness of significant estimates made by management? How does the auditor challenge these estimates?
- What top three areas did the independent auditor spend the most time discussing with management during the reporting period? How satisfied is the committee that management is cooperative and forthcoming with requested information and documentation in these areas and that management was able to produce the information requested?
- Does the independent auditor use technology such as automation, data analytics, and machine learning to improve the effectiveness and efficiency of its audits?
- Is the independent auditor delivering value and insights to management and the committee beyond the audit?
- Does the committee meet separately with the independent auditor outside the presence of management? Meet separately with individual members of management? Meet separately with the internal auditor?

Additional notes

PCAOB Spotlight suggesting questions that may be of interest to audit committee members to consider among themselves or in discussions with their independent auditors.

Communication between the audit committee and the external auditor

The external auditor is required by the International Standards on Auditing (ISAs) 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 external 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 which are 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 include:
  - Management's initial selection of, or changes in, significant accounting policies or the application of such policies in the current period
  - 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, and
    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

ACTION ITEM:
Audit committees together with management should ensure all related parties and their transactions (transactions being the transfer of resources, services, or obligations between related parties, regardless of whether a price is charged) are correctly identified.

Clear notes

Questions to consider: Related parties

- What are the business reasons for the transaction? Are these reasons in line with the company's overall strategy and objectives?
- Are the terms of the transaction consistent with the market? In other words, would these terms apply to an unaffiliated party?
- When and how will the transaction be disclosed? How will investors view the transaction when it is disclosed?
- What impact will the transaction have on the financial statements?
- Which insiders could benefit from the transaction, and in what way?
- Are outside advisers needed to help understand the implications of the transaction?

Additional notes

Communication between the audit committee and the external auditor (continued)

- 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 may 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 significant 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 where 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 report 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 external auditor generally communicates the following to the audit committee:

- Key audit matters
- 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.

Recommendations for communications with the external auditor

- Meet to review and discuss with the external auditor the company's annual audited financial statements and interim financial statements, including disclosures in management's discussion and analysis
- Periodically, meet separately with the external auditor, management, and the internal auditors
- Obtain a formal written communication from the external auditor regarding independence and other matters annually
- Review with the external auditor any audit problems or difficulties and management's response
- Set clear hiring policies for employees or former employees of the company's external auditor

Appointment of the external auditor

All companies that are subject to a mandatory audit must appoint a registered (in terms of the ***Auditing Professions Act***), independent auditor at every annual general meeting. This requirement will also apply to those companies that voluntarily elected to comply, and provided for such requirement in their Memorandum of Incorporation.

The audit committee must nominate an auditor, which it regards as independent from the company (see above), to the shareholders for appointment. Where the shareholders elect to appoint a different auditor, the appointment will only be valid if the audit committee has verified that the auditor is independent.

Where a firm is appointed as auditor, the audit committee must also verify the independence of the individual that will be responsible for the audit (the designated auditor). The name of the designated auditor must be included in the register as contemplated in **Section 85** of the ***Companies Act***.

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.

The independence rules are different for entities governed by the US and Securities Exchange Commission (SEC). For such entities the **SEC rules** should be referred to.

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 (on page)**
  - **Family and personal relationships (on page)**
  - **Employment relationships (on page)**
  - **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.

Personal 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.

ACTION ITEM:
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 interests.

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 allowed to 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 external 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 the position being filled.

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

Business relationships

The rule prohibits an external 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 external 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 pre-approved by the audit committee.

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 on whether the non-audit services are 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 (PIEs).

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

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 are set out. Both the person responsible for the audit as well as the audit firm are prohibited from providing accounting, bookkeeping 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 or audit firm will be disqualified from appointment.

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 provisions of the ***Companies 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. 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 **IRBA** introduced mandatory audit firm rotation (MAFR) effective from 1 April 2023. In terms of this regulation the audit firm may not accept the appointment as auditor if that firm has served as the auditor of that company for more than 10 consecutive financial years on or after 1 April 2023. The audit firm will only be eligible for appointment as auditor after a cooling off period of five years.*

At the time of publishing the MAFR rule has been set aside by Supreme Court of Appeal.

ACTION ITEM:
The audit committee needs to request the auditor and management to provide detail with respect to the non-audit services provided by the auditor prior to appointment, and specifically consider whether or not the auditor (or any other member of the audit firm) provided any of the prohibited services (bookkeeping, accounting, related secretarial services, maintenance of financial records or preparation of the financial statements) to the company in the preceding five years.

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. In doing so, the audit committee should evaluate inspection results from audit regulators and consider audit quality indicators (AQIs), if available.

Evaluation of the external auditor

Because there is no formal guidance regarding the evaluation of the external auditor and because needs and preferences vary by company and audit committee, practices for evaluating the external 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 external auditor, many conduct some form of evaluation to make decisions on auditor appointment and retention. As noted previously, **Section 94** of the ***Companies Act*** established the audit committee's responsibility for the appointment, compensation, and oversight of the external 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. The party responsible for coordinating the evaluation should obtain information not only from the audit committee, but from senior financial management and the internal auditors. Depending on the size and structure of the company, it may be appropriate to obtain input from the management of significant operating locations or business units.
- **Form and nature of the assessment**
  Some external 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 external auditors.
- **Assessment criteria**
  The criteria for evaluating the external 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

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. These programmes 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 programmes 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 programme 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 programme of continuing education, the board should identify risks and complex issues facing the organisation and even possibly the industry, depending on how specialised the industry is. 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 programme. 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 as well. 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.

Leading practices for Board education

- Provide orientation of new members with executives and external auditors
- Consider offering continuing education programmes 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

Once a curriculum is set, the board, the audit committee, and management should assess the resources available to create and deliver the programme. The programme 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 programmes 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.

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. External auditors or outside consultants can assist in identifying appropriate specialists.

Clear notes

Questions to consider: ESG

- Where does the primary oversight responsibility for ESG reside on the board, both overall and in terms of its various components (for example, climate, diversity, talent, cyber)?
- Is there consistent understanding of where and when these elements are being discussed at the board and committee level?
- How is the organisation kept aware of developments in ESG legislation and regulations in relevant jurisdictions for the business?
- How is management considering the organisation's environmental goals and related activities for reporting purposes (for example, the business, risk factors, and results of operations sections in SEC filings)?
- What climate-related information is currently gathered and reported? What level of assurance is currently obtained over this information? What additional information (if any) would need to be developed or gathered (including for disclosure in the audited financial statements)?
- How does the company evaluate the materiality of climate-related disclosures? What systems and processes are in place for gathering the necessary information for determining whether such disclosures are material?
- If the company issues a sustainability report, to what extent has the audit committee reviewed the report prior to issuing, and how has management walked through the key assumptions made and the basis for the metrics and goals disclosed?
- If the organisation discloses climate-related information in the annual report that contains or accompanies the financial statements, such as in the management discussion and analysis section, how consistent are those disclosures with the audited financial statements? What internal controls over financial reporting are in place to address the disclosure that would be required in the audited financial statements?

Additional notes

Please refer to **Appendix E**.

Clear notes

Questions to consider: Mergers & Acquisitions

- How does the deal affect the future returns on equity and assets as well as the projected growth trajectory of the newly combined entity following the transaction?
- How has the due diligence preceding a transaction considered risks and compliance associated with environmental, health, safety, legal, and regulatory standards that might affect financial statements of the combined new entity following the transaction?
- How is management relying on qualified subject matter experts and other advisers as appropriate through the deal process?
- To what extent has management adopted a post-merger plan for integrating the newly combined business units and processes?
- To what extent has management considered the importance of the culture and the control environment as part of its integration plan?

Additional notes

Clear notes

Questions to consider: Cyber

- Where does the primary oversight responsibility for cyber risk reside on the board? If responsibility is delegated to the audit committee, has the board considered calling this risk out specifically in the audit committee charter?
- To what extent does management understand where its most sensitive information is kept and how it is stored, used, and protected?
- To what extent do management and the board leverage cyber simulations to assess the effectiveness of the organisation's cyber response plan and make improvements?
- How are cyber assessments conducted on the organisation's operational technology? Do assessments highlight the business impact of an operational technology breach?
- How have cyber attacks escalated, and what controls have been reassessed as a result, including those related to an evolving talent model (for example, with a remote or hybrid workforce)?
- How does the organisation assess its cyber risk profile internally or externally to identify areas where digital finance transformation, ESG, and other new or quickly shifting requirements and initiatives may pose risks?
- How do leadership, structure, capabilities, and resources support a comprehensive focus on cyber risks?
- How effectively would an enterprise response plan and a ransomware playbook or checklist be implemented quickly if needed?
- How proactive is management in identifying and complying with all the laws and regulations that govern data capture, use, retention, security, and disposal?
- How has internal audit considered cyber risk in the development of the internal audit plan?
- Does the audit committee have the appropriate capabilities, knowledge and experience to oversee the cyber risks?

Additional notes

Audit committee performance evaluation

King IV requires the board to perform regular performance evaluations, 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 external 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 external auditor, the internal auditors, and senior financial executives
- Whether the audit committee raises the right questions with management and the external auditor, including questions that indicate its understanding of critical accounting policies and judgements
- Whether the audit committee has been responsive to issues raised by the external 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

Deloitte has developed a template to assist audit committees in drafting an appropriate performance evaluation. Best practice has been selected from a number of existing evaluations and relevant literature, such as the ***Companies Act*** and ***King IV***. The sample is included as **Appendix C**.

View a sample audit committee performance evaluation.

Clear notes

Questions to consider: Evaluation and self-assessment

- Should an objective third party be engaged to assist in the process for a fresh perspective?
- Is the grading scale similarly understood by all participants of the evaluation process? Are participants encouraged to provide qualitative feedback?
- Are the results of the assessment discussed with the committee? Is an actionable plan developed based on identified opportunities and areas of concern?
- Have we leveraged the assessment results as a catalyst to influence where the audit committee spends its time?
- Have the results of the evaluation been shared with the board? Has feedback on individual committee members been shared with those committee members?

Additional notes

Appendices

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 IV Report on Corporate Governance for South Africa 20169 (King IV)***. 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.

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ACTION ITEM:
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 issuers, including investment companies, small-business issuers, and foreign private issuers. Many of the items presented here are not applicable to voluntary filers. 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

a. The audit 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.

b. Except with respect to the appointment, fees and terms of engagement of the external 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. Members 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.

c. 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.

d. 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.

e. The audit committee is appointed by the shareholders of the company for the primary purpose of assisting the board in:
   i. Ensuring the continued independence of the external auditor
   ii. Overseeing the external audit process
   iii. Applying the combined assurance model to ensure a coordinated approach to all assurance activities
   iv. Reviewing the expertise, resources and experience of the finance function
   v. Considering the appropriateness of the expertise and experience of the financial director
   vi. Overseeing the internal audit function
   vii. Oversight of internal controls and financial reporting
   viii. Financial risk assessment and oversight

f. 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 external auditor, financial and senior management, the internal audit function, and the board of directors.

2. Membership

a. The committee shall be appointed annually by the shareholders at the annual general meeting and shall comprise at least three members.

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

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

d. The audit committee must consist of at least three members. Each member of the committee must be a director of the company and not:

  i. Be involved in the day to day management of the company for the past financial year

  ii. Be a full-time employee of the company for the past 3 financial years

  iii. 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

  iv. Be related to anybody who falls within the above criteria.

e. 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.

f. 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.

g. 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.

h. The external auditors shall be invited to attend meetings of the committee on a regular basis.

3. Secretary

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

4. Quorum

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

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

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

b. 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.

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

7. Minutes of meetings

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

b. 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.

c. 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 external auditors and the Chief Audit Executive (CAE).

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

8. Annual General Meeting

a. Members of the committee will be appointed by the shareholders at the Annual General Meeting.

b. The chairman of the committee shall attend the Annual General Meeting 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:

a. 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 external 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;

b. Ensure that the appointment of the auditor complies with the ***Companies Act***, the ***Auditing Profession Act*** and other relevant legislation;

c. Oversee the relationship with the external auditors including (but not limited to):
   - Determining their remuneration, whether fees for audit or non-audit services;
   - Approving their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;
   - 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, length of audit firm tenure and rotation of the designated auditor;
   - 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);
   - Agreeing with the board a policy on the employment of former employees of the company's auditors, then monitoring the implementation of this policy;
   - 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;
   - Assessing annually their qualifications, expertise and resources and the effectiveness of the audit process which shall include a report from the external auditors on their own internal quality procedures;
   - Considering the risk of the withdrawal of the company's auditors from the market; and
   - At least annually, obtaining and reviewing a report by the external auditor describing:
     - The external auditor's internal quality-control procedures;
     - 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 external auditor, and any steps taken to deal with such issues; and
     - All relationships between the external auditor and the company

d. Meet regularly with the external auditors, including once at the planning stage before the audit and once after the audit at the reporting stage. The committee shall meet the external auditors at least once a year, without management being present, to discuss their remit and any issues arising from the audit;

e. Review and approve the annual audit plan and ensure that it is consistent with the scope of the audit engagement;

f. Review the findings of the audit with the external auditors. This shall include but not be limited to, the following:
   - A discussion of the significant audit issues which arose during the audit;
   - 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;
   - Any accounting and audit judgements; and
   - Levels of errors identified during the audit.

g. Review the effectiveness of the audit process annually;

h. Review any representation letter(s) requested by the external auditors before they are signed by management;

i. Review the management letter and management's response to the auditors' findings and recommendations;

j. Distinguish between audit and non-audit services, and develop and implement a policy on the supply of non-audit services by the external auditors, taking into account any relevant ethical guidance on the matter;

k. Pre-approve the contracts for non-audit services to be rendered by the external auditor and consider whether the auditor's provision of non-audit services is compatible with the auditor's independence; and

l. 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:

a. 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

b. 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;***

c. Ensure that a combined assurance model is applied to provide a coordinated approach to all assurance activities, and in particular:
   - Ensure that the combined assurance received is appropriate to address all the significant risks facing the company;
   - Support the integrity of information used for internal decision-making by management, the governing body and its committees, and; support the integrity of the organisation's external reports, and
   - Monitor the relationship between the external assurance providers and the company;

d. Understand the scope of the internal and external auditors' review of internal control over financial reporting (ICFR) and obtain reports on significant findings and recommendations, together with management responses;

e. 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:
   - 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
   - Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal controls;

f. 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;

g. Review analyses prepared by management and/or the external auditor setting forth significant financial reporting issues and judgements made in connection with the preparation of the financial statements;

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

i. 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:

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

b. The methods used to account for significant or unusual transactions where different approaches are possible;

c. Whether the company has followed appropriate accounting standards and made appropriate estimates and judgements, taking into account the views of the external auditors;

d. The clarity of disclosure in the company's financial reports and the context in which statements are made; and

e. 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 Whistleblowing and fraud

The committee shall:

a. 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;

b. 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 external auditor; and

c. 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:

a. 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;

b. Approve the appointment and removal of the CAE;

c. 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;

d. Approve the internal audit charter and perform an annual review of the charter, making recommendations for changes if required;

e. Review and approve the annual internal audit plan;

f. 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;

g. Review all reports on the company from the CAE, including managements responsiveness to findings and recommendations;

h. 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

i. Perform an annual assessment of the internal audit function's responsibility, budget and staffing, with input from the external auditor.

9.5 Reporting responsibilities

a. 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.

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

c. 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.

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

King IV proposes that the following information relating to the functioning of the audit committee is provided (usually as part of the audit committee report in the governance section of the integrated report):

- Its overall role and associated responsibilities and functions;
- Its composition, including each member's qualifications and experience;
- Any external advisers or invitees who regularly attend committee meetings;
- Key areas of focus during the reporting period;
- The number of meetings held during the reporting period and attendance at those meetings;
- Whether the committee is satisfied that it has fulfilled its responsibilities in accordance with its terms of reference;
- A statement as to whether the audit committee is satisfied that the external auditor is independent of the organisation. The statement should specifically address:
  - The policy and controls that address the provision of non-audit services by the external auditor, and the nature and extent of such services rendered during the financial year;
  - The tenure of the external audit firm and, in the event of the firm having been involved in a merger or acquisition, including the tenure of the predecessor firm;
  - The rotation of the designated external audit partner; and
  - Significant changes in the management of the organisation during the external audit firm's tenure which may mitigate the attendant risk of familiarity between the external auditor and management.
- Significant matters that the audit committee has considered in relation to the annual financial statements, and how these were addressed by the committee;
- The audit committee's views on the quality of the external audit, with reference to audit quality indicators such as those that may be included in inspection reports issued by external audit regulators;
- The audit committee's views on the effectiveness of the chief audit executive and the arrangements for internal audit;
- The audit committee's views on the effectiveness of the design and implementation of internal financial controls, and on the nature and extent of any significant weaknesses in the design, implementation or execution of internal financial controls that resulted in material financial loss, fraud, corruption or error
- The audit committee's views on the effectiveness of the CFO and the finance function;
- The arrangements in place for combined assurance and the committee's views on its effectiveness;
- 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:

a. 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;

b. Be provided with appropriate and timely training, both in the form of an induction programme for new members and on an ongoing basis for all members;

c. At least once a year, review the appropriateness of the expertise, experience and adequacy of resources of the company finance function;

d. Oversee any investigation of activities which are within its terms of reference and act as a court of the last resort; and

e. 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:

a. To conduct investigations into any matters within its scope of responsibility;

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

c. 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;

d. 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;

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

f. 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

g. 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 with regard to its statutory duties of verifying the independence of the external auditor, determining the fee for the external auditor, and for the terms of engagement of the external auditor.

Appendix B: Audit committee calendar planning tool

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 IV*** 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 IV*** 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.

ACTION ITEM:
All companies should consult with legal counsel regarding the applicability and implementation of the various activities identified.

Clear months

	Results from						Meeting month											
Action/Responsibility	Companies Act 2008	King IV	JSE Listings	Other requirement	Common practice	Suggested frequency	January	February	March	April	May	June	July	August	September	October	November	December
General responsibilities																		
Review audit committee members' compliance with applicable independence rules and regulations.	●					Annually and as needed												
As necessary, engage outside legal, accounting, or other advisers and provide funding to compensate those advisers.		●			●	As needed												
Report regularly to the board of directors regarding the execution of duties and responsibilities.		●			●	Each board meeting												
Review the financial literacy and expertise of all audit committee members. Determine audit committee financial expert status and determine that members are in compliance with applicable rules and regulations.	●	●			●	Annually												
Conclude each regular audit committee meeting with an executive session of the committee, without members of management.					●	Each audit committee meeting												
Periodically, meet with management privately to discuss any necessary matters.		●			●	Quarterly												
Consider and plan for succession of audit committee members					●	Annually												
Review, with management, the company's finance function, including its budget, organisation and quality of personnel		●	●		●	Annually												
Review of financial/controls information																		
Review and discuss with management and the external auditors the company's annual financial statements prior to filing.		●		●		Annually												
Review the internal auditor's assessment of internal controls.		●				Annually												
Review other reports rendered by the external auditors and submitted by the company to any governmental body or the public.					●	As needed												
Discuss the financial information and earnings guidance provided to analysts and ratings agencies. This discussion may be in general terms.		●			●	Annually												
Review regular internal reports to management prepared by the internal audit function and management's response.					●	Semi-annually												

Clear months

Action/Responsibility	Results from: Companies Act 2008	King IV	JSE Listings	Other requirement	Common practice	Suggested frequency	Meeting month: January	February	March	April	May	June	July	August	September	October	November	December
External auditor relationship																		
Nominate an external auditor for appointment by the shareholders.	●	●	●			Annually												
Compensate, retain, and oversee the work of the external auditor for the purpose of preparing or issuing an audit report or related work.	●	●				Ongoing												
Review the performance of the external auditor, including the lead audit partner. Ensure that partners are rotated in accordance with applicable requirements.	●	●			●	Annually												
Pre-approve audit and non-audit services provided by the external auditor.	●	●				In accordance with policy (as necessary)												
Consider the independence of the auditor, including engaging in dialogue with the external 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.	●	●			●	Annually and as needed												
Oversee the resolution of disagreements between management and the external auditor if they arise.		●				As needed												
Review with the external auditor any problems or difficulties encountered in the course of the audit and management's response.					●	Annually												
Review the audit plan and scope with the external auditor.				●		Annually												
Review written communications between the external auditor and management, including (but not limited to) the management letter and schedule of unadjusted differences.				●		As reported by the external auditor												
Periodically, meet with the external auditor privately to discuss any matters necessary.		●			●	Quarterly												

Action/Responsibility	Results from: Companies Act 2008	Results from: King IV	Results from: JSE Listings	Results from: Other requirement	Results from: Common practice	Suggested frequency	Meeting month: January	February	March	April	May	June	July	August	September	October	November	December
Financial reporting processes, accounting policies, and internal control																		
In consultation with the external 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).			●		●	Quarterly												
In consultation with the external auditor and the internal audit function and management, review the combined assurance model.		●				Annually												
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.					●	Quarterly												
Review management's analyses of financial reporting issues and judgements made in connection with the preparation of the financial statements.					●	Quarterly												
Review with management the effect of regulatory and accounting initiatives, as well as off-balance-sheet structures, on the financial statements of the company.					●	As needed												
Review and approve all related-party transactions.					●	Quarterly												
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.	●	●			●	Annually												
Receive and review reports or complaints of questionable accounting, auditing, or internal control matters.	●	●			●	Semi-annually or quarterly												

Clear months

Action/Responsibility	Results from: Companies Act 2008	King IV	JSE Listings	Other requirement	Common practice	Suggested frequency	Meeting month: January	February	March	April	May	June	July	August	September	October	November	December
Internal audit activities																		
Review and advise on the selection or removal of the Chief Audit Executive.		●	●		●	As needed												
Periodically, meet with Internal Audit privately to discuss any necessary matters.		●			●	Quarterly												
Periodically, review with Internal Audit any significant difficulties, disagreements with management, or scope restrictions encountered in the course of the function's work.					●	Annually												
Review the activities and organisational structure of the internal audit function, as well as the qualifications of its personnel.		●			●	Annually												
Review the internal audit charter and plan and recommend any necessary changes.		●			●	Annually												
Periodically review, with Internal Audit, the internal audit function's responsibilities, budget, and staffing.		●			●	Annually												
Risk management																		
Discuss with management significant risk exposures, including major financial and accounting risk exposures, and the steps taken by management to control them.		●			●	Annually												

Clear months

Action/Responsibility	Results from: Companies Act 2008	Results from: King IV	Results from: JSE Listings	Results from: Other requirement	Results from: Common practice	Suggested frequency	Meeting month: January	February	March	April	May	June	July	August	September	October	November	December
Other responsibilities																		
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	●	●																
Integrated reporting process: (i) Consider all factors and risks that may impact on the integrity of the integrated report (ii) Review the annual financial statements (iii) Comment in the annual financial statements on the financial statements, the accounting practices and the effectiveness of the internal financial controls (iv) Review the disclosure of sustainability issues in the integrated report to ensure that it is reliable and does not conflict with the financial information		●																
Review the audit committee charter; recommend to the board of directors any necessary amendments, as conditions dictate.		●			●	Annually												
Review, with the external 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.					●	Annually												
Participate in appropriate continuing education.					●	As needed												
Assess performance relative to the audit committee's purpose, duties, and responsibilities.		●			●	Annually												

Appendix C: Audit committee performance evaluation (self-assessment)

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. Leave blank if the statement is not applicable or you do not have enough information to rank the audit committee on that particular item.

- 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. This tool should not be viewed as a substitute for such professional advice or services, nor should it 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 this tool.
- 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 who relies on it. All companies should consult with qualified and professional advisers and/or legal counsel regarding the applicability and implementation of the various activities identified.

Clear form

Composition and quality	Strongly disagree				Strongly agree
1. Qualified audit committee members are identified by sources independent of management (e.g., independent board members assisted by an outside search firm).	1	2	3	4	5
2. Audit committee members have the appropriate qualifications to meet the objectives of the audit committee charter, including appropriate financial literacy.	1	2	3	4	5
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.	1	2	3	4	5
4. The audit committee demonstrates appropriate industry knowledge and includes a diversity of experiences and backgrounds.	1	2	3	4	5
5. Members of the audit committee meet all applicable independence requirements.	1	2	3	4	5
6. The audit committee participates in a continuing education programme to enhance its members' understanding of relevant accounting, reporting, regulatory, auditing, and industry issues.	1	2	3	4	5
7. The audit committee monitors compliance with corporate governance regulations and guidelines.	1	2	3	4	5
8. The audit committee reviews its charter annually to determine whether its responsibilities are described adequately and recommends changes to the board for approval.	1	2	3	4	5
9. New audit committee members participate in an orientation programme to educate them on the company, their responsibilities, and the company's financial reporting and accounting practices.	1	2	3	4	5
10. The audit committee chair is an effective leader (e.g., runs committee meetings efficiently and effectively, stays coordinated with the board and other committees, keeps open lines of communication with management, internal audit, and independent auditor, etc.).	1	2	3	4	5
11. The audit committee, in conjunction with the nominating committee (or its equivalent), creates a succession and rotation plan for audit committee members, including the audit committee chair.	1	2	3	4	5

Additional notes

Clear notes

Clear form

Understanding the business, including risks	Strongly disagree				Strongly agree
12. The audit committee considers significant risks that may directly or indirectly affect financial reporting, even in instances where such risks are overseen by the full board or other committees. Examples include: • Regulatory and legal requirements • Concentrations (e.g., suppliers and customers) • Market and competitive trends • Financing and liquidity needs • Financial exposures • Business continuity • Cybersecurity • Company reputation • Financial strategy execution • Financial management's capabilities • Management override • Fraud control • Company pressures, including "tone at the top"	1	2	3	4	5
13. The audit committee considers, understands, and approves the process implemented by management to effectively identify, assess and respond to the organisation's risks.	1	2	3	4	5
14. The audit committee understands and approves management's fraud risk assessment and has an understanding of identified fraud risks.	1	2	3	4	5
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.	1	2	3	4	5

Additional notes

Clear notes

Clear form

Process and procedures	Strongly disagree				Strongly agree
16. The audit committee reports its proceedings and recommendations to the board after each committee meeting.	1	2	3	4	5
17. The audit committee develops a calendar that dedicates the appropriate time and resources needed to execute its responsibilities.	1	2	3	4	5
18. Audit committee meetings are conducted effectively, with sufficient time spent on significant or emerging issues.	1	2	3	4	5
19. The level of communication between the audit committee and relevant parties is appropriate; the audit committee chair encourages input on meeting agendas from committee and board members, management, the internal auditors, and the independent auditor.	1	2	3	4	5
20. The audit committee sets clear expectations and provides feedback to the full board concerning the competency of the meetings to allow audit committee members sufficient time to study and understand the information.	1	2	3	4	5
21. The audit committee has input into the succession planning process for the CFO.	1	2	3	4	5
22. The agenda and related information (e.g., prior meeting minutes, press releases, financial statements) are circulated in advance of visits to company locations with members of management.	1	2	3	4	5
23. Written materials provided to audit committee members are relevant and concise.	1	2	3	4	5
24. Meetings are held with enough frequency to fulfill the audit committee's duties and at least quarterly, which should include periodic.	1	2	3	4	5
25. Regularly, audit committee meetings include separate private sessions with management and the internal and independent auditors.	1	2	3	4	5
26. The audit committee maintains adequate minutes of each meeting.	1	2	3	4	5
27. The audit committee and the compensation committee regularly review management incentive plans to consider whether the incentive process is appropriate.	1	2	3	4	5
28. The audit committee meets periodically with the committee responsible for reviewing the company's disclosure procedures.	1	2	3	4	5
29. The audit committee respects the line between oversight and management of the financial reporting process.	1	2	3	4	5
30. Audit committee members come to meetings well prepared.	1	2	3	4	5

Clear form

Oversight of the financial reporting process, including internal controls	Strongly disagree				Strongly agree
31. The audit committee considers the quality and appropriateness of financial accounting and reporting, including the transparency of disclosures.	1	2	3	4	5
32. The audit committee reviews the company's significant accounting policies.	1	2	3	4	5
33. The audit committee understands and approves the process used by management to identify and disclose related-party transactions.	1	2	3	4	5
34. The audit committee has a process for reviewing quarterly and annual earnings releases, including pro forma or non-GAAP information and other significant financial information or earnings guidance, with management and the independent auditor.	1	2	3	4	5
35. The audit committee oversees the organisation's external financial reporting and internal control over financial reporting. This oversight includes a process for reviewing all reports before they are issued and providing comments to management and the independent auditor when applicable.	1	2	3	4	5
36. The audit committee reviews the processes related to financial statement certifications made by the CEO and the CFO.	1	2	3	4	5
37. 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.	1	2	3	4	5
38. The audit committee understands and gives appropriate consideration to the internal control testing conducted by management, the internal auditors, and the independent auditor to assess the process for detecting internal control issues or fraud. Any significant deficiencies or material weaknesses that are identified are addressed, reviewed, and monitored by the audit committee.	1	2	3	4	5
39. The audit committee makes inquiries of the independent auditor, internal auditors, and management on the depth of experience and sufficiency of the company's accounting and finance staff.	1	2	3	4	5
40. 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.	1	2	3	4	5
41. The audit committee oversees that management takes action to achieve resolution when there are repeat comments from auditors, particularly those related to internal controls.	1	2	3	4	5
42. Adjustments to the financial statements that resulted from the audit are reviewed by the audit committee, regardless of whether they were recorded by management.	1	2	3	4	5
43. The audit committee is consulted when management is seeking a second opinion on an accounting or auditing matter.	1	2	3	4	5

Clear form

Oversight of audit functions	Strongly disagree				Strongly agree
44. The audit committee understands the coordination of work between the independent and internal auditors and clearly articulate its expectations of each.	1	2	3	4	5
45. 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).	1	2	3	4	5
46. The audit committee oversees the role of the internal audit director from selection to termination (e.g., appointment, evaluation, involve management will be brought to the attention of the audit committee.	1	2	3	4	5
47. 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.	1	2	3	4	5
48. The audit committee appropriately considers internal audit reports, management's responses, and steps toward improvement.	1	2	3	4	5
49. The audit committee oversees the role of the independent auditor from selection to termination and has an effective process to evaluate the independent auditor's qualifications and performance.	1	2	3	4	5
50. The audit committee considers the independent audit plan and provides recommendations.	1	2	3	4	5
51. The audit committee reviews the audit fees paid to the independent auditors.	1	2	3	4	5
52. The audit committee comprehensively reviews management's representation letters to the independent auditor, including making inquiries about any difficulties in obtaining the representations.	1	2	3	4	5
53. The audit committee pre-approves all audit and non-audit services provided by the independent auditor and considers the scope of the non-audit services provided.	1	2	3	4	5
54. The audit committee reviews other professional services that relate to financial reporting (e.g., consulting, legal, and tax strategy services) provided by outside consultants.	1	2	3	4	5
55. The audit committee monitors the process to determine that the independent auditor's partners are rotated in accordance with applicable rules.	1	2	3	4	5
56. The audit committee has private sessions with management and the internal and independent auditors that result in candid discussion of pertinent issues.	1	2	3	4	5

Clear form

Ethics and compliance	Strongly disagree				Strongly agree
57. Audit committee members oversee the process and are notified of communications received from governmental or regulatory agencies related to alleged violations or areas of noncompliance.	1	2	3	4	5
58. The audit committee oversees management's procedures for enforcing the company's code of conduct.	1	2	3	4	5
59. The audit committee determines that there is a senior-level person designated to understand relevant legal and regulatory requirements.	1	2	3	4	5
60. The audit committee oversees the organisation's hotline or whistleblower process, reviews the log of incoming calls that relate to possible fraudulent activity, and understands the procedures to prohibit retaliation against whistleblowers.	1	2	3	4	5

Clear form

Monitoring activities	Strongly disagree				Strongly agree
61. 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.	1	2	3	4	5
62. The company provides the audit committee with sufficient funding to fulfill its objectives and engage external parties for matters requiring external expertise.	1	2	3	4	5

Additional notes

Clear notes

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 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 is applicable, to ensure that there are no unresolved issues of concern

The audit committee of a Public Entity must, among 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 ***MFMA***, 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.

Appendix E: Climate and the audit committee

The audit committee frontier – addressing climate change.

The headlines

Audit committees find themselves in the climate spotlight. They are viewed as responsible for clarity in how companies report climate commitments and measure progress: Countries have made commitments under the Paris Agreement; companies have also made their own commitments and need to measure and communicate progress against these; investors are asking for accurate data to be able to assess opportunities, risks, emissions, and other climate impacts; regulators are seeking higher standards in ESG reporting to eradicate "greenwashing" and "social washing"; and NGOs are increasingly pointing out shortcomings in this high stakes and fast moving area of company reporting.

The crux of the matter is that climate must be integrated with company strategy. From this integration commitments can be made, which, in turn, reorient the whole business with a re-articulated purpose – leading to adjustments to business operations, control processes, metrics, and reporting.

Many directors are now considering climate impacts when reviewing operational performance, budgets, forecasts, capital expenditure, and mergers and acquisitions – and many companies are also now prioritising climate impacts when reshaping stressed supply chains. Traditional procurement functions, still focused on price and quality, will now include carbon as a decision criterion.

Directors serving on audit committees, viewed by shareholders and others as the "reporting arbiters" at companies, may not be experts in this area – but they rapidly need to become climate literate. What does this mean? It implies not only a good understanding of their company's operations and their impact on our planet (including third parties in the value chain) but also a solid understanding of both reporting requirements and emerging standards. The responsibilities of audit committees in relation to risk and internal control, internal and external assurance also need to reflect climate impacts. This entails no small investment of time from the director, and moreover, it requires reliable information flows from management as discussed later. Market scanning of good practices as they emerge will help the pack learn from the pioneers.

Does the audit committee need to shift its focus?

It's an important question. Independent estimates suggest that over 90% of the value of companies is now represented by intangibles. The value of business critical assets such as people, technology, know-how, and brand value are all underpinned by trust and confidence, which now requires reliable and informative ESG reporting. Reputations, in turn, can be tarnished – and tarnished quickly – by ESG reporting that turns out not to be true.

The traditional deep focus areas for audit committees is the scrutiny of judgments and estimates in the financial statements – and here audit committees should shift focus to some degree – at the very least to ensure that the potentially significant impact that climate change can have on asset valuations and completeness of liabilities is appropriately reflected in the financial statements that the company discloses.

But the oversight responsibilities of audit committees may need to extend further: All directors should now also embrace how companies describe their business model and its resilience in the face of climate change, including existing and emerging climate-related risks. Some companies may need to change their business models entirely or they may face extinction. Where this is the case, it requires careful consideration as to how the strategy and milestones for this transition should be described to investors.

How does climate affect the audit committee's responsibilities?

The Task Force on Climate-Related Financial Disclosures (TCFD) recommended disclosures, illustrated below, are a useful way of thinking about climate for audit committees. These 11 key disclosures under four areas are explored in more detail in TCFD publications and case studies.

TCFD's 11 recommended disclosures

Governance	Strategy	Risk Management	Metrics and Targets
Disclose the organization's governance around climate-related risks and opportunities.	Disclose the actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning where such information is material.	Disclose how the organization identifies, assesses, and manages climate-related risks.	Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.

Recommended Disclosures	Recommended Disclosures	Recommended Disclosures	Recommended Disclosures
• Describe the board's oversight of climate-related risks and opportunities.	• Describe the climate-related risks and opportunities the organization has identifies over the short, medium, and long term.	• Describe the organization's process for identifying and assessing climate-related risks.	• Describe the metrics used by the organization to assess climate-related risks and opportunities in line with its strategy and risk management process.
• Describe management's role in assessing and managing climate-related risks and opportunities	• Describe the impact of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning.	• Describe the organization's processes for managing climate-related risks.	• Disclose Scope 1, Scope 2, and if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks.
	• Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios.	• Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organization's overall risk management.	• Describe the great targets used by the organization to manage climate-related risks and opportunities and performance against targets.

Source: Implementing the recommendations of the Task Force on Climate-related Financial Disclosures, TCFD, 2021

Recommendation

The diagram reflects Deloitte's thinking about the key aspects of the audit committee's remit in relation to climate in reference to the recommendations of the TCFD. It may be a useful starting point and helpful to consider when reviewing your audit committee charter and agendas.

How the audit committee's responsibilities on climate address the TCFD

Key audit committee responsibilities:

Corporate Reporting	Risk and Internal Control	Internal Assurance	External Audit
• Quality of required disclosures including on material risks, opportunities and strategic decisions • Asset and liability valuations • Clarity around governance structures, management's role and where decision-making responsibility sits	• Identifying and evaluating existing principal risks and emerging risks over the short, medium and long term • Resilience of the business to potential climate-related threats (including use of scenario analysis) • Business-specific governance and internal controls	• Suitable focus on climate-related risks and processes underlying the risk identification, assessment and management • Appropriate expertise available • Level of assurance over climate-related management information • Level of assurance over climate related KPI's and targets, especially as they impact executive remuneration	• Level of assurance over climate-related data and analysis • Impact of climate change on the financial statements adequately reflected in audit plan • Impact of change on going concern risk fully understood, where relevant

Changes in the audit committee's responsibilities: corporate reporting

With its focus on the integrity of corporate reporting, the climate literate audit committee will want to be able to judge for itself that all material climate-related risks, opportunities, and strategic decisions have been clearly incorporated in recognition, measurement, and disclosure. This is no small task in any business, whether in manufacturing, energy and resources, or services.

Audit committees will want to ensure that climate matters have been appropriately reflected in asset and liability measurement where material – this will involve an assessment of whether management's forward-looking assumptions and forecasts in respect of the climate-related risks and opportunities are robust and appropriately reflect the company's climate commitments and strategies. Many leading companies have chosen to disclose a carbon price assumption voluntarily, although not currently required by reporting standards. Where one is used, disclosure is recommended; those that do not currently disclose a carbon price should consider the increasing demands to do so. Does the business use a carbon price in its investment appraisal and what carbon price is assumed in future forecasts?

Climate scenarios (e.g., Paris-aligned scenarios) will need to evaluate the different implications of medium and long-term scenarios across the entire value chain, not just in the operations that the company owns and controls. Audit committees will want to ensure that there is consistency of this scenario planning with the assumptions used in the forecasts which underpin impairment and other balance sheet recognition and measurement decisions.

This modelling could prove to be complex and involve a number of hypotheses of future action and variations in carbon price.

The recommendations of the TCFD draw out the importance of the quality of climate governance at companies and place the board at the heart of the review and approval of all the TCFD disclosures. This emphasis on governance includes scenario analysis and ESG reporting. Audit committee members will also want to understand how climate decision-making takes place within the company, and to satisfy themselves that what is reported by the company reflects realities on the ground. This points to responsibilities and accountabilities throughout the organisation – and about whether this is clearly described. Disclosures should seek to enhance stakeholders' understanding of the impacts of climate change on the company's performance over time.

In driving clear and robust corporate reporting, the audit committee will need to consider materiality. This is still financial materiality – but audit committees will need to consider longer time horizons and consider the entire value chain in considering materiality. And audit committee members may wish to consider how and whether the company's activities and business practices could exacerbate risks to enterprise value (for example, overuse of a resource that is essential to the ability of the company to generate enterprise value). The audit committee will want to think about areas such as trend information, and whether the key performance indicators (KPIs) presenting trends – in the annual report or elsewhere - are suitable and not misleading, as well as the figures themselves. For example, carbon per employee may be declining while overall carbon emissions might very well be on the rise. The board and committee members will want to have a deep understanding of how impacts can arise in the value chain and affect the business over time.

Another problem is an organisational one. The audit committee is used to dealing primarily with the finance function, but climate- related information often comes from outside the finance function. This means that climate reporting requires integrated thinking. The data involved relates to the organisation as a whole – and many organisations are not yet sufficiently "joined up" in terms of thinking to provide audit committees with a clear line of sight. Suitable ownership and reporting structures need to be established; data may need to be scrubbed (data outside finance can be less reliable and may take some time to refine); and established internal control frameworks may need to be adapted to include carbon impacts. The number of companies tracking carbon through a carbon budget and then analysing performance is currently very small. Yet it is increasingly recognised as important; audit committees should consider how they can judge carbon performance without this tool.

"Our ask is that companies provide adequate disclosure and articulate strategic changes that may impact progress, either negatively or positively. These short, medium, and long-term targets will allow everyone to track progress and identify innovative leaders."

Changes in the audit committee's responsibilities: risk and internal control

At the heart of the matter is business decision-making. The audit committee will want to be confident that the company identifies and monitors current and emerging material climate-related risks, covering both physical and transition risks, to inform business decisions. Measurement and reporting on progress towards established targets are essential for accountability and addressing any concerns about resilience. This, in turn, requires an appropriate climate governance framework, with clear parameters and appropriate adaptation of the internal controls framework to enable climate vulnerabilities to be uncovered and for timely relevant data to inform the business strategic response.

Changes in the audit committee's responsibilities: internal assurance

The audit committee will want to have confidence regarding the quality of the management information used in the company's climate analysis – both for decision-making but also in corporate reporting for climate and TCFD disclosures. Audit committees will want to hear from executives how managers in the business are being upskilled to deal with climate-related risks and opportunities as part of the core business. They will also want to understand how the Chief Internal Auditor plans to upskill team members to provide appropriate challenge to management and help build confidence in climate-related management information through internal assurance.

"Audit committees play a key role ensuring that the quality of information on sustainability factors, including on climate change, is comparable and meets the standards of financial information."

Changes in the audit committee's responsibilities: external audit

It is not just the audit committee that stands under the climate spotlight; external auditors are in a similar position. The audit committee should evaluate how climate-related matters have been incorporated into the work of the external auditor, along with any planned use of specialists and whether the external auditor has been provided with the information needed to identify and respond to climate-related risks to financial statements, and to assess adequacy and quality of the disclosure.

The auditor's final report to the audit committee should indicate the auditor's conclusions, material observations, and any difficulties encountered in undertaking the work they set out to perform.

It is also worth considering whether climate-related KPIs and disclosures that are outside the scope of the audit are critical to understanding business performance and resilience and should be subject to reasonable or limited scope assurance. Assurance can help build trust in the reported information.

Should the audit committee have this climate knowledge itself or ensure instead that expert advice is available to it on a regular basis?

Boards will reach different judgments on how to bring in expertise across the range of subjects within its remit. Now that climate is integral to the audit committee agenda, the audit committee also needs to ensure that expertise is available and being delivered in an effective way.

It is essential that audit committees understand specifically how climate impacts (or can impact) the company and how that relates to enterprise value. It is therefore important that they have the knowledge to articulate the financial impacts of climate change, as called for by TCFD.

"We should not underestimate the complexity of climate change. For boards, addressing this complexity can be daunting, but we do not believe that it is simply a matter of placing specialists in the audit committee."

A final word

This area is moving fast: business models, supply chains, company policies, reporting standards, and data availability all need to be on the radar to ensure the audit committee is alive to emerging issues and to enable prompt and informative reporting on the financial impacts of climate change.

In its review of its own effectiveness, the audit committee will want to include assessment of its own climate competence as part of its regular review of skills and knowledge requirements. There will likely be gaps to fill through learning and development, and possibly succession planning, too. This sounds like a lot to consider, and it is. Addressing the climate challenge requires leadership and sustained effort over many years.

Clear notes

Questions to consider: Climate and the audit committee

The expertise of the audit committee

- Does the audit committee chair drive a proactive approach to high-quality climate reporting?
- Does the audit committee as a whole have climate competence?
- Has the audit committee received relevant training on industry context on climate change, accounting for climate in the financial statements (including forecasting), and disclosure in line with recognised standards such as TCFD and SASB?

Audit committee meetings and terms of reference

- Is climate a specific topic on the audit committee agenda? If so, is it given sufficiently frequent attention?
- Does the audit committee conduct appropriately detailed "deep dives" into climate, including in relation to the most critical areas and judgments?
- Has the audit committee's role regarding climate-related matters been recognised in its terms of reference, or charter?

Oversight of accounting judgments, business and financial reporting, and other company announcements

- Is the audit committee confident that it receives sufficiently robust management information and metrics (both financial and non- financial)?
- Does the audit committee consider the level of internal or external assurance on climate-related matters published by the company?
- Has the audit committee assessed management forecasting and scenario testing on climate-related risks in light of recognised scenario data, the industry circumstances, and the business model?
- Has the audit committee considered disclosure of the carbon price assumption behind financial judgments?
- Does the audit committee review all information outside the annual financial statements, for example, TCFD disclosures, to ensure it is both reliable and consistent with information used in preparing the financial statements?

Risk management and internal control

- Does the audit committee consider that the company's procedures for identifying emerging risks can be successful in identifying and assessing material climate-related risks, covering both physical and transition risks?
- Has the audit committee ensured that there is an appropriate climate governance framework, with clear parameters and appropriate adaptation of the internal controls framework, so that controls around business decisions support the company's climate objectives?
- In the risk area, has the audit or risk committee confirmed that the business is undertaking a proper inventory of its assets or operations to assess climate vulnerabilities and that the business is addressing any resilience issues identified?

Additional notes

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