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Governance in focus

Audit committees and the 2017 reporting season

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A year of great change

Foreword from William Touche

Dear Audit Committee Member,

Since our round up mid-year, the world has changed dramatically, in politics and financial markets. We are seeing the UK government, the FRC and of course companies responding. There is much to consider and as always, the Deloitte Academy is here to guide directors on the changes to think about as you approach year end reporting.

The vote to leave in June has had a number of very visible impacts on governance and reporting. Highlighting just a few: the BEIS Select Committee consultation will be followed by the BEIS Department's own consultation on various board and company governance matters; the FRC is calling for boards to report to shareholders in annual reports on how, in fulfilling their responsibilities, they have addressed the wider stakeholder considerations set out in s172 of the Companies Act; the fall in sterling is affecting operating activities in many sectors and the increase in bond yields and commodity volatility is affecting asset valuations; overall, forecasting is becoming more difficult. However, of course, volatility and uncertainty also creates opportunity. Looking forward, where previously we were expecting a three year gap between revisions to the UK Corporate Governance Code, we now expect Code changes in 2017, a year after the 2016 Code.

Annual reports of UK listed companies have advanced hugely over the last few years. This year most companies are embracing the 2016 Code changes and the 2016 Guidance for Audit Committees. Audit committee reports will therefore be substantially revised this year for these matters as well as for the EU audit regulations.

Investors and the FRC also want more detail in certain key areas: first, more granularity in business model and risk management disclosures addressing best practices from the Financial Reporting Lab; and second, more detail on critical judgements, including information about the sensitivity of judgements to changes in assumptions, with explanations of the possible impact of changes on the following year's results. This latter point picks up the concern from the Investment Association in their letter to listed company chairmen for greater ownership by boards as a whole of company forecasts in light of the increase in unexpected profit warnings and asset write-downs.

You and your companies will also be looking at your first reports under the Modern Slavery Act 2015 and Gender Pay Gap reporting, which brings us neatly to the topic of culture and values, on which the FRC has issued guidance for boards. The market valuation of a company is increasingly recognised to be in its intangible assets – its mission, people, culture, innovation, and business system – and investors and regulators are keen to see more of this portrayed in the annual report.

In closing, we believe it is critical that companies continue to have a forward-looking approach. The company of tomorrow will need to be a transparent and proactive business, embracing technology and promoting development both of individuals and being a responsible citizen within society at large. This itself will start companies on the road to enhance public trust in business.

This year end round up addresses all these matters and guides you to where more useful material can be found. Do get in touch with your Deloitte partner or our Deloitte governance team if you would like to discuss any areas in more detail. And don't forget you can join us at the Deloitte Academy where we host live updates, which allow you the opportunity to air current issues and swap notes with your peers – even more useful at a time of great change and uncertainty. The Deloitte Academy website also has all of our publications and useful checklists.

Yours faithfully,

William Touche
Vice-Chairman
Leader of Deloitte UK Centre for Corporate Governance

Key areas of focus for this year's annual report

Deloitte.

The Deloitte Academy
November 2016

Governance *in brief*

FRC's CRR report calls for more tax and stakeholder reporting as well as better business model, risk and judgment disclosures

Headlines

- Compliance with the accounting framework is generally good and the introduction of the strategic report has improved the quality of narrative reporting
- Not all companies provide sufficient balance in their reporting and this undermines the quality of corporate reporting and erodes trust
- The summary findings of the recent thematic review on tax reporting highlights the importance of high quality information in effective tax rate reconciliations and clear articulation of how companies account for tax uncertainties
- The report encourages companies to consider how they might report on how the directors have discharged their duty under s172 of the Companies Act (to promote the success of the company for the benefit of its members whilst having regard to other stakeholders)
- Looking forward, Brexit could have significant implications for both individual company reporting and for the future adoption of IFRS
- Separately, the FRC has issued a year-end advice letter to audit committee chairs and finance directors, highlighting key areas for consideration during the preparation of the annual report this coming reporting season, which are also covered in this report

The FRC's Corporate Reporting Review

Summary

The FRC's report provides an overview of the Corporate Reporting Review (CRR) team's activities for the year ended 31 March 2016. The FRC reports that compliance with the accounting framework is generally good and the introduction of the strategic report has improved the quality of narrative reporting. However, not all companies provide sufficient balance in their reporting and this undermines the quality of corporate reporting and erodes trust.

The FRC continues to focus on its Clear & Concise initiative aiming to encourage good communication in corporate reporting. It explains that directors should give "the same level of attention to removing immaterial disclosures as to ensuring that all material information is included" and that, although some points may continue to be raised in FRC letters, directors are expected to have sufficient confidence in their own decisions to justify them.

Key findings from the review: financial statements

Accounting policies
Accounting policies should be specific and granular. Revenue recognition policies should link clearly to the company's business model disclosures in the strategic report. Complex long-term contracts such as outsourcing contracts should be explained in detail, including exactly when and how revenue is measured.

Critical judgements and sources of estimation uncertainty
Reporting should include specific, concise explanations covering the specific judgements the board has made and how uncertainty or changes to estimates could affect the next year's accounts, including sensitivities or ranges of potential outcomes.

Tax
Companies should disclose the amount of uncertain tax provisions and explain tax uncertainties more clearly by explaining the bases for recognition and measurement. The thematic review of companies' tax disclosures highlighted the value of greater visibility of the factors underlying effective tax rate reconciliations.

Pension disclosures
Pension disclosures should adequately explain the risks to which the company is exposed by the pension plan and the disclosure of the plan's assets should clearly reflect the nature of the plan's investments.

The audit committee's challenge of the robustness of management forecasts underlies both the assessment of longer term viability and many of the significant judgements affecting financial reporting. The pervasive nature of forecasting means they underpin numerous areas of the financial statements, from asset valuations to taxation.

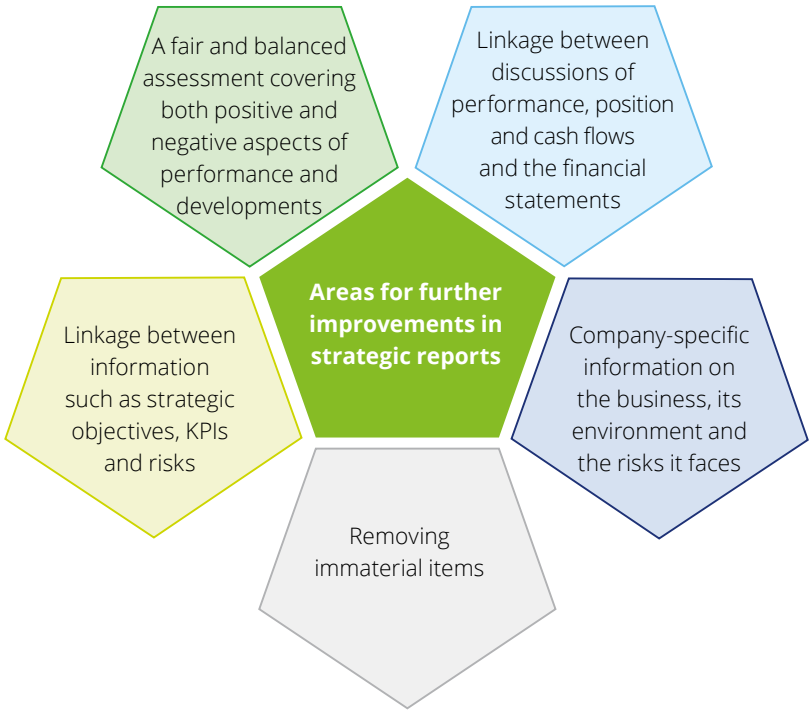
Key findings from the review: strategic reports

One of the most common areas of challenge was whether reports are **sufficiently balanced and comprehensive**. This refers to including information of particular interest to investors, such as effective tax rates and non-financial key performance indicators, in addition to not giving too much emphasis to alternative performance measures (APMs) or pro-forma information prepared on a non-GAAP basis. Companies are also encouraged to provide better explanations of how they carried out the process underlying their **viability statement** and the supporting analysis.

Other areas of interest

Other areas the FRC mentions as important are:

- Clear articulation of the **business model**.
- The quality of reporting around **principal risks and uncertainties**.
- **Tax arrangements**, including tax strategies, whether tax rates are sustainable and whether any material tax risks are clearly described in the annual report.
- Sufficient explanation around **dividend disclosures**, where better disclosure would link how dividend policies operate in practice to risks and capital management decisions.
- Reporting the risks of the **UK decision to exit the European Union**.
- Sufficiently meeting the needs of wider stakeholders, which could include a clear description of the company's **culture, values and behaviour expectations** and an assessment of how they are measured.
- Reporting concisely on **how directors have discharged their duty to have regard to other stakeholders**, as required by section 172 of the Companies Act 2006.



FRC's year-end advice letter

The FRC also issued a letter of advice to audit committee chairs and finance directors:

- The potential impact of **low interest rates** on the amounts reported in the financial statements – in particular long term assets and liabilities, with perhaps the greatest impact on pension scheme liabilities and suppressed returns on pension scheme assets.
- The need for **disclosures regarding major IFRS standards that will become effective in the near future**, in particular IFRS 15 Revenue from Contracts with Customers, IFRS 9 Financial Instruments and IFRS 16 Leases. Comparative periods for IFRS 15 and IFRS 9 will commence from 1 January 2017 and the FRC expects that companies will have made substantial progress on implementation and should provide information on this and any significant likely impacts of the new standards.

Deloitte View

- In this report, the FRC is reflecting the political agenda and the social mood by encouraging business to enhance tax disclosures and include disclosures on wider stakeholder considerations set out in the Companies Act in the reporting of the discharge of director responsibilities.
- There is a welcome call for a focus on culture, values and human capital – reflecting investor recognition that human capital is fundamental in value creation.
- The FRC is right to comment on the dangers of the low interest rate environment within the context of the IFRS fair value framework.
- There is also a focus on quantifying judgements and uncertainties which, with increased economic uncertainty, is a useful communication tool for directors and investors regarding key assumptions used in judgements about the future.
- Alternative Performance Measures are going to see further scrutiny this year, in part because the ESMA guidelines, which took effect for public statements published on or after 3 July, enhance regulatory focus in this area.
- Finally, it is good to see the ongoing progress in corporate reporting being recognised – annual reports have certainly come on a long way in the last few years.

Alternative Performance Measures

ESMA's Guidelines on Alternative Performance Measures (APMs) are now fully in force. They apply to financial APMs disclosed in regulated information made available to the market in accordance with the requirements of the Transparency Directive and the Market Abuse Regulation and prospectuses published on or after 3 July 2016.

In the UK, the FRC will monitor compliance with the guidelines which require that:

- APMs should not be displayed with more prominence, emphasis or authority than, or distract from, measures directly stemming from financial statements;
- each APM should have a meaningful, well defined label;
- each APM should be reconciled to its most directly reconcilable item in the financial statements;
- an explanation should be provided as to why an APM is considered to provide useful information; and
- APMs should be presented consistently from period to period with comparative information provided.

Our publication **Alternative performance measures: A practical guide** provides additional guidance on the use of APMs, setting out what is considered best practice and providing real-life examples of how entities present such measures.

Audit committee reporting

The Guidance on Audit Committees, dated April 2016, recommends a number of new disclosures designed to reflect the changes in the 2016 UK Corporate Governance Code and also to meet the needs of investors more directly and reflect the findings of the FRC's Financial Reporting Lab's project on **Reporting of Audit Committees** (issued in October 2013):

- How the audit committee composition requirements have been addressed.
- How the performance evaluation of the audit committee has been conducted.
- The current external audit partner's name and for how long the partner has held the role.
- Advance notice of any plans for retendering of the external audit.
- The committee's policy for approval of non-audit services.
- The audit fees for the statutory audit of the company's consolidated financial statements and the fees 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.
- For each significant engagement, or category of engagements, an explanation of the services provided and why the audit committee concluded that it was in the interests of the company to purchase them from the external auditor.
- 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 nature and extent of interaction (if any) with the FRC's Corporate Reporting Review team.
- When a company's audit has been reviewed by the FRC's Audit Quality Review team, disclosures about significant findings and the resulting actions they and the auditors plan to take. This disclosure should not include the audit quality category awarded.

These disclosures are expected to be included in the audit committee report within the annual report and unfortunately there is no indication in the Guidance that it is acceptable to provide any of the disclosures on a website. However, the Guidance does say that the section need not repeat information disclosed elsewhere in the annual report, as long as 'signposts' are provided to the information. This will be helpful for boards seeking to keep information on matters such as the annual performance evaluation of the board and its committees in the same place.

A challenge for drafting audit committee reports will be ensuring that all of the new disclosures remain fresh each year and do not introduce too much repetitive material.

Business model reporting Summary

In October 2016, the FRC's Financial Reporting Lab published **Business model reporting**, which provides insight for companies on the importance of business model information to investors and the type of information they look for.

Key findings

Although some companies may feel that business model disclosure is only a compliance exercise, investors were unanimous that business model information is fundamental to their analysis and understanding of a company and its prospects, and that a lack of good disclosure around the business model may raise concerns over the quality of management. They would like business model disclosures to be written in plain, clear, concise and factual language, avoiding a promotional or aspirational tone.

Some investors have remarked that the articulation of the business model is often clearer and more detailed in company investor day slide packs, or for some companies, on the corporate website. Ideally a company would develop one high quality disclosure and use it consistently across the different reporting channels, whilst also reporting any changes to the business model clearly, with the rationale explained and detail on any further known upcoming changes.

As business model information provides context for the other information in the annual report most investors want it positioned towards the front of the Strategic Report. In addition:

- where a company operates a number of business models, **disclosure about each significant business model** is helpful;
- investors are looking for **better natural linkage** of business model information to other sections of the Strategic Report, and consistency with disclosure in the annual report; and
- they would like **more detail** than is currently provided by most companies. In particular, investors find disclosures are often lacking information that answers questions such as:
  - What are the key revenue and profit drivers and how do profits convert to cash?
  - Are there any key asset and liability items that support the business model?
  - What is the company's competitive advantage?

The report indicates that adding this specific information would not be expected to increase the number of pages taken up by the business model, instead asking for the description of the business model to be a more focused disclosure with "relevant factual information".

The effect of 'Brexit' on UK regulation

The FRC's CRR report, discussed above, highlights the fact that, whilst the UK remains in the EU, UK reporting remains subject to the EU legislative framework. This means that:

- application of IFRSs 'as endorsed for use in the European Union' remains a legal requirement, meaning that new or revised standards cannot be adopted before EU-endorsement; and
- the FRC remains a competent authority of an EU member state, tasked with monitoring and supervising compliance with ESMA's common enforcement priorities, which therefore remain relevant for UK company reporting.

In the longer term, the possible effect of Brexit on financial reporting requirements is less clear. The FRC annual review raises the possibility of the UK assessing international standards for adoption itself and states that a review will be conducted over the coming months to identify risks and opportunities for improvement in corporate reporting arising from exiting the EU, stating also that:

- the FRC continues to support the application of a single set of high quality global financial reporting standards by listed companies, but that support is contingent on the standards being of sufficient quality and capable of implementation at appropriate cost; and
- the UK should continue to be influential in the development of IFRSs following exit from the European Union.

Deloitte's Annual Report Insights 2016

Summary

As in previous years, Deloitte has undertaken a comprehensive survey of 100 UK listed companies' annual reports, reviewing, amongst other things, disclosures on risk management, principal risks, the longer term viability statement, audit committee reporting and non-GAAP measures. The full survey is available from www.deloitte.co.uk/annualreportinsights together with a highlights document, which includes ideas on how to improve annual reports in the upcoming reporting season and pulls out areas of regulatory focus, as well as identifying some key pitfalls to avoid.

Overall comments

On average, annual reports got longer by **8 pages**.

8 companies *described their reports as integrated.*

Only **13%** *of companies displayed a comprehensive level of linkage*

34 *companies referred to materiality in their annual report, but only* **3** *companies clearly described the process they went through to determine financial statement materiality*

33% *of companies discussed how they create value for a variety of stakeholder groups*

Risk management and principal risks

There was a new requirement effective for companies surveyed this year to make a statement regarding the robust assessment of principal risks, and also to monitor risk management and internal control systems on an ongoing basis.

Surprisingly. only **85%** *of companies made a clear statement regarding the robust assessment of principal risks – as required by the 2014 Code – but, of these companies, in our opinion* **12%** *of accompanying risk management disclosures were insufficient to corroborate that statement.*

Likewise. only **85%** *of companies had disclosures that made it clear that the board monitors risk management and internal control systems on an ongoing basis.*

78% *of companies discussed principal risks or risk management in the first* **20%** *of their annual report – sufficient prominence of risk disclosures is an area of regulatory focus.*

16% *of companies identified Brexit as a principal risk in their last annual report.*

Non-GAAP measures

The ESMA Guidelines and the FRC's approach to implementing these in the UK indicate a step-change in the UK approach to disclosure, moving the UK closer to the worldwide regulatory position. Some further detail is given on page 4. This area no doubt will create a new tension between communication and compliance. The challenge will be to achieve both.

76% *of companies used APMs in the summary section of their annual report.*

Of these companies:

72% *failed to give equal or greater prominence to corresponding GAAP measures.*

63% *failed to provide clear reconciliations to financial statement line items.*

13% *failed to provide comparatives.*

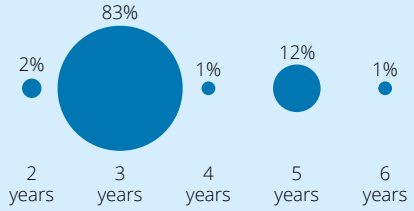
The longer term viability statement – a change last year

This was a new requirement in the 2014 Code and we therefore updated our previous research to look at a range of listed companies reporting throughout the year. 73% of companies considered their longer term viability statement of sufficient importance to include it in the strategic report – this also has the benefit of linking it more clearly to risk management and principal risks. Audit committees should bear in mind that the viability statement should be the subject of a new exercise (and disclosure) each year.

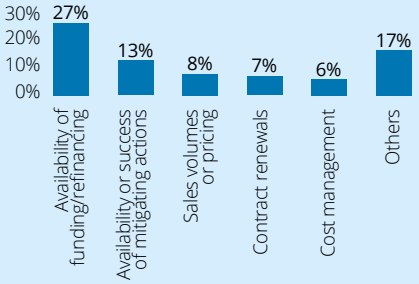
Only **92%** *of companies met the Code requirement to explain the reason for the lookout period they chose.*

52% *did not include the qualifications or assumptions underlying the directors' assessment of longer term viability.*

What lookout period have companies used?



Reporting of qualifications or assumptions



Corporate culture

Some key areas of focus for corporate governance continue to be corporate culture and succession planning, building trust in the organisation. We also considered the board's response to the increased threat from cyber crime.

Only **11%** *of companies surveyed included specific discussion around how the board owns and drives corporate culture in their corporate governance report.*

26% *included discussion of activities underlying their corporate culture in the strategic report.*

Audit committee reporting

With the new Guidance on Audit Committees and the first year of reporting in line with the Competition & Markets Authority's Order on the audit market, we looked at some of the disclosures required by both.

Just **65%** *of companies surveyed that were subject to the requirements included a statement of compliance with the Competition & Markets Authority's Order regarding audit tendering.*

However, **87%** *of companies included disclosure around the tenure of the incumbent auditor and 49% of companies disclosed advance notice of plans to retender the external audit – as required by the 2016 Code.*

Only **2** *companies indicated that their annual report had been reviewed by the FRC's Corporate Reporting Review team. A few stated explicitly that theirs had not been reviewed.*

20% *of companies indicated that they had taken account of the FRC's Audit Quality Review team's report on their auditors.*

Cyber risk

43% *of companies referred to the board's involvement in activities related to cyber risk and security – up from* **32%** *in 2015.*

Succession planning

Only **58%** *of FTSE 100 companies,* **26%** *of FTSE 250 companies and* **5%** *of smaller companies included clear disclosures around succession planning.*

Contacts – Corporate reporting

Deloitte's corporate reporting team advises on how to better meet the needs of your company, industry regulators, investors and the wider public.

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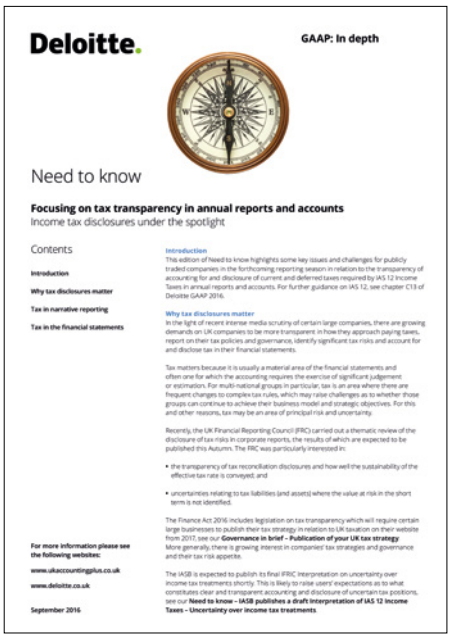
Ever-increasing focus on transparency in taxation



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GAAP: In depth

Need to know

Focusing on tax transparency in annual reports and accounts
Income tax disclosures under the spotlight

Contents

Introduction

Why tax disclosures matter

Tax in narrative reporting

Tax in the financial statements

For more information please see the following websites:

www.ukaccountingplus.co.uk

www.deloitte.co.uk

September 2016

Introduction

This edition of Need to know highlights some key issues and challenges for publicly traded companies in the forthcoming reporting season in relation to the transparency of accounting for and disclosure of current and deferred taxes required by IAS 12 Income Taxes in annual reports and accounts. For further guidance on IAS 12, see chapter C13 of Deloitte GAAP 2016.

Why tax disclosures matter

In the light of recent intense media scrutiny of certain large companies, there are growing demands on UK companies to be more transparent in how they approach paying taxes, report on their tax policies and governance, identify significant tax risks and account for and disclose tax in their financial statements.

Tax matters because it is usually a material area of the financial statements and often one for which the accounting requires the exercise of significant judgement or estimation. For multi-national groups in particular, tax is an area where there are frequent changes to complex tax rules, which may raise challenges as to whether those groups can continue to achieve their business model and strategic objectives. For this and other reasons, tax may be an area of principal risk and uncertainty.

Recently, the UK Financial Reporting Council (FRC) carried out a thematic review of the disclosure of tax risks in corporate reports, the results of which are expected to be published this Autumn. The FRC was particularly interested in:

- the transparency of tax reconciliation disclosures and how well the sustainability of the effective tax rate is conveyed; and
- uncertainties relating to tax liabilities (and assets) where the value at risk in the short term is not identified.

The Finance Act 2016 includes legislation on tax transparency which will require certain large businesses to publish their tax strategy in relation to UK taxation on their website from 2017, see our **Governance in brief – Publication of your UK tax strategy**. More generally, there is growing interest in companies' tax strategies and governance and their tax risk appetite.

The IASB is expected to publish its final IFRIC Interpretation on uncertainty over income tax treatments shortly. This is likely to raise users' expectations as to what constitutes clear and transparent accounting and disclosure of uncertain tax positions, see our **Need to know – IASB publishes a draft Interpretation of IAS 12 Income Taxes – Uncertainty over income tax treatments**.

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The Deloitte Academy
July 2016

Governance *in brief*

Publication of your UK tax strategy

Headlines

- All multinational businesses with UK operations and consolidated turnover in excess of €750 million, or UK registered companies, partnerships and permanent establishments with turnover in excess of £200 million or gross assets in excess of £2 billion are required to publish their tax strategy in relation to UK taxation.
- The legislation applies to financial years commencing on or after the date of Royal Assent to the law. For December year ends this will mean publication of the UK tax strategy before the end of December 2017.
- Businesses are expected to follow the internal approval processes they would normally follow for public statements, including approval by the Board.
- The vast majority of businesses affected believe that this new legislation will lead to additional work for them.

Background

The 2016 Finance Bill includes revised legislation on tax transparency which requires large businesses within its scope to publish their tax strategy in relation to UK taxation on their website before their financial year-end. At the end of June 2016, HMRC published its final guidance on areas to consider when drafting the UK tax strategy.

This is part of a trend of ever-increasing demands for transparency of the tax arrangements of large businesses. In December we published **Governance in brief: The Global Tax Reset and the Reporting of Tax in Annual Accounts**. This examined some of the approaches being taken worldwide to tax transparency.

In the UK, the disclosure of UK tax strategy is part of an ongoing drive for greater transparency in this country, demanded by government, regulators, the media and the public. In January 2016 George Osborne, the Chancellor of the Exchequer, called for agreement for the country-by-country reporting of taxation to be made publicly available. In addition, the FRC, in its current review of the quality of disclosure around tax, is encouraging ever-greater levels of clarity and explanation in the management discussion, in accounting policies as well as in the detailed notes to the financial statements on both uncertainties and other factors affecting taxation.

Key developments

The Finance Act 2016 received Royal Assent on 15 September 2016. This brought into law the requirement for the largest UK businesses to publish their UK tax strategy and also introduced a mechanism to make country-by-country reporting a public report, although this is not yet operative and it is uncertain whether or when the mechanism will be used. The existing regulations require country-by-country Reporting to be made available privately to the tax authorities only.

In addition, the FRC has conducted a thematic review into reporting on taxation, which reported in late October 2016. Our Need to know publication provides more detail on issues concerning the reporting of tax.

The existing regulations require country-by-country reporting to be made available privately to the tax authorities only for accounting periods beginning on or after 1 January 2016.

Publishing your UK tax strategy

The legislation applies to financial years commencing on or after 15 September 2016. For December year ends this means publication of the UK tax strategy before the end of December 2017.

All multinational businesses with consolidated turnover in excess of €750 million and with UK operations, or UK registered companies, partnerships and permanent establishments with turnover in excess of £200 million or gross assets in excess of £2 billion are required to publish their UK tax strategy on their websites. The strategy information must be made available on the internet so as to be accessible to the public free of charge on an ongoing basis and needs to be updated periodically.

The minimum information which must be made publicly available in relation to the group, sub-group, company or partnership is:

- the approach to risk management and governance arrangements in relation to UK taxation;
- the attitude towards tax planning (so far as affecting UK taxation);
- the level of risk in relation to UK taxation that it is prepared to accept; and
- the approach towards its dealings with the UK tax authorities.

HMRC has published guidance which includes suggestions for what should be included under each heading, which we expect will be considered when HMRC Customer Relationship Managers (CRMs) and others review the contents of the UK tax strategy. A summary of this guidance is available in our Governance in brief.

Businesses are expected to follow the internal approval processes they would normally follow for public statements, including approval by the Board.

FRC thematic review of tax disclosures

The FRC has recently published its findings of the review of tax disclosures of 33 FTSE 350 companies. As explained when the project was launched in December 2015, the objective of the review was to "encourage more transparent reporting of the relationship between tax charges and accounting profit and factors that could affect that relationship in the future, in accordance with existing requirements".

The FRC has stated that tax is an area they will continue to monitor, but key points coming out of their review are as follows:

Looking forward to 2017

During 2017 the introduction of a corporate offence for the criminal facilitation of tax evasion is expected. This could expose companies to unlimited financial penalties where they have not taken reasonable steps to prevent those who acted on its behalf from committing the criminal facilitation.

Tax evasion
Tax evasion is being knowingly concerned in, or in taking steps with a view to, the fraudulent evasion of a tax.

Contacts – Tax

Our tax team specialises in providing advice on international tax developments, including global tax regulation and transparency initiatives.

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Key messages

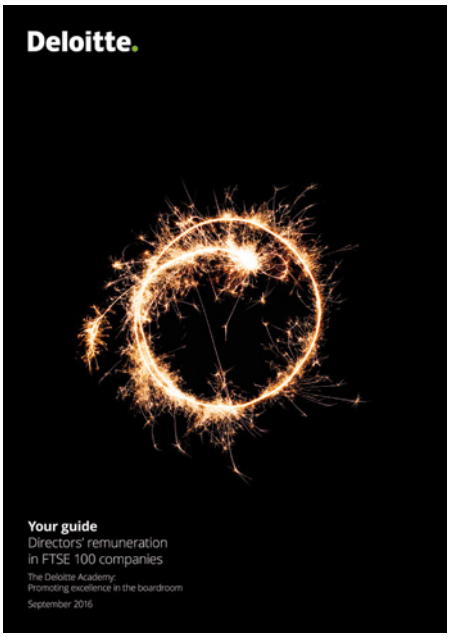
There was evidence of improvements in the transparency of tax disclosures included in strategic reports. Those reports that demonstrated good practice provided more detail on material tax matters likely to be important to investors including discussion of important tax issues arising in the year, major tax risks facing the company and explanations of the reassessment of prior year tax estimates where these were significant and tax impacts of acquisitions. There was also an increase in companies providing disclosures describing their general approach to tax reporting.

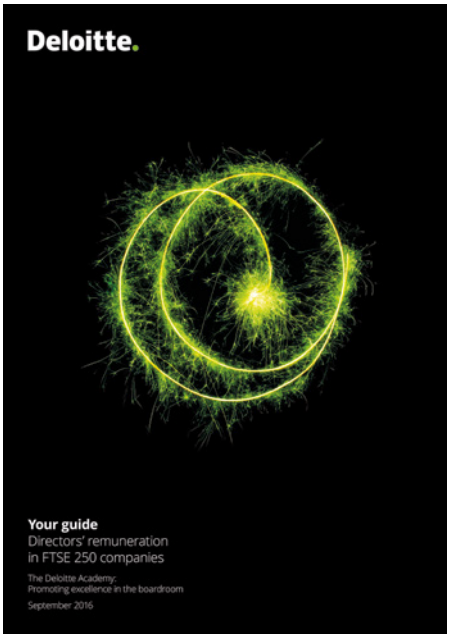
Better reports discussed the effective tax rate including commentary on variances in the effective tax rate on the prior year, key factors influencing the effective tax rate and the expected future rate. This information provided greater visibility of the factors affecting the tax charge and its sustainability.

There is scope for companies to articulate better how they account for tax uncertainties by explaining the bases for recognition and measurement. The FRC will continue to challenge companies who do not provide disclosures of the amount of uncertain tax provisions when these are subject to risk of material change in the following year. Better disclosures covered when provision is recognised, how the provision is measured and the factors considered in determining the amount to be provided.

Companies can improve the usefulness of their disclosure of significant judgements and estimation uncertainties relating to tax by considering which information about specific judgements and estimation uncertainties would be most useful to the user of the accounts. These could cover, for example, the nature of the assumption or uncertainty, a quantification of the carrying amount of the asset or liability subject to the uncertainty and include sensitivity analysis or a range of possible outcomes to provide users with a better understanding of the issue.

Achieving 'clear and concise' remuneration reporting





A continuing area of focus

Remuneration issues continue to attract high levels of interest from the media and the general public. As with previous years, high profile cases have been at the forefront of reporting and, with recent events, shareholder voting has become a highly politicised issue. Some commentators are calling this the second shareholder spring, making comparisons to 2012 when a number of high-profile companies received low levels of support.

Some investors have responded to ongoing public concern around executive pay. The Executive Remuneration Working Group was set up in September 2015, aiming to identify potential reforms to executive pay. A number of investor groups have updated their guidelines to reflect the findings contained in the Working Group's final report, which was published in July 2016. Most notably, and most recently, the Investment Association updated their Principles of Remuneration in October 2016 in order to incorporate the Working Group's findings.

In addition, the GC100 and Investor Group has published a revised 2016 version of its Directors' Remuneration Reporting Guidance. Some details of the updates are below and more information can be found in our publications on FTSE 100 and FTSE 250 remuneration, available on the Deloitte Academy's website. The FRC has emphasised that investors are looking for "clear and concise" remuneration reporting and recommended that companies should read the GC100 and Investor Group's Guidance.

Although the initial "snapshot" of gender pay gap is still to be taken in April 2017, the final regulations providing the detail on exactly how reporting should take place have not been released. They are expected imminently and we will issue a Governance in brief on the topic once they are available.

The 2016 AGM season

We analysed the 2016 AGM season at the point where over 75% of FTSE 350 companies had held their AGMs. This is the last season before many companies will be required to resubmit their remuneration policy for approval again next year.

Remuneration issues continue to attract high levels of interest from the media and the general public. As with previous years, high profile cases have been at the forefront of reporting and, with recent events, shareholder voting has become a highly politicised issue. Some commentators are calling this the second shareholder spring, making comparisons to 2012 when a number of high-profile companies received low levels of support.

This year, 90% of FTSE 100 companies received more than 80% of votes in favour of the remuneration report. However, the number of companies receiving in excess of 90% of votes in favour is much lower than at any time since 2008 – so there is still work to do to ensure proxy agencies and shareholders are in agreement with companies and feel fully informed in advance.

Investment Association Principles of Remuneration

The Investment Association issued an update of its Principles of Remuneration and an accompanying open letter to FTSE 350 remuneration committee chairmen in October 2016. The key areas of focus were:

- The Principles reflect the findings contained in the Final Report of the Executive Remuneration Working Group (ERWG), which was published in July 2016. The Principles now include sections on levels of remuneration and shareholder consultation.
- A stronger emphasis on setting executive pay arrangements in the context of pay for the wider workforce, including recommending the disclosure of pay ratios.
- The continued focus on full retrospective bonus target disclosure (i.e. threshold, target and maximum) and the target setting process.

The revised Principles and open letter can be found here and the Principles are also available at www.ivis.co.uk/guidelines.

Directors' remuneration reporting guidance 2016

The GC100 and Investor Group's revised guidance now encourages remuneration committees to consider:

- feedback from shareholders on the last report and whether this suggests that the disclosures could be set out more clearly;
- what would make it clearer to assess and understand each section of the report; and
- whether the thinking and purpose behind the remuneration committee's decisions is clear.

Other areas of update in the guidance include:

- the need to explain the link between remuneration and strategy, with suggested alignment and cross-referencing between the remuneration report and the strategic report;
- the application of flexibility, discretion and judgement to ensure that the remuneration outcome balances management performance and the shareholder experience;
- any decision to rely on the commercial sensitivity carve-out to justify the non-disclosure of performance targets should only be used where the directors positively form the opinion that company-specific circumstances mean the performance target or measure in question is commercially sensitive;
- retrospective disclosure of targets, including the full range of threshold, target and maximum, is expected at the end of the reported year or, where commercial sensitivity remains an issue, at a later time. Where it will be disclosed at a later time, investors generally expect a commitment in the remuneration report as to when that time will be;
- where no payments to past directors or in respect of loss of office have been made, the report should include a "nil return" to confirm this fact;
- where retrospectively disclosing the percentage change in the remuneration of the CEO against a comparator, companies should consider using a meaningful comparator group of employees, not, for example, a narrow group consisting of senior managers; and
- if a company wishes to put forward a new policy to investors mid-cycle, investors generally expect a coherent rationale for doing so.

Contacts – Executive remuneration

Deloitte's executive remuneration practice helps clients develop executive remuneration strategies in line with corporate objectives and advises remuneration committees on the corporate governance and regulatory framework that applies to executive remuneration in the UK.

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Harnessing corporate culture to support a clear business purpose

> "Culture exists regardless. If left to its own devices, it shapes itself, with the inherent risk that behaviours will not be those desired. Employees will work out for themselves what is valued by the leaders to whom they report."
>
> **Sir Anthony Salz**

Deloitte.

The Deloitte Academy
July 2016

Governance *in brief*

FRC reinforces the importance of corporate culture

Headlines

- A strong and transparent corporate culture is a valuable asset and can protect and generate value.
- A healthy corporate culture starts with clear alignment of business purpose, values, strategy and incentives where people at all levels of an organisation understand the values of the organisation and act in accordance with those values.
- Corporate culture is led by the board and is not about rules but about actions. A key challenge for boards, and for executives, is to model the behaviours they want to see in the business and to find constructive ways to encourage and build those behaviours.
- The importance of high quality, insightful reporting both to the board and externally to investors and other stakeholders in the annual report is another key focus of this report, which suggests drawing in HR, Internal Audit, risk and compliance, the company secretary and the external auditor as contributors to the board's understanding of culture throughout the organisation.
- The FRC will use the observations in this report, and any feedback received, to update the Guidance on Board Effectiveness, which was last updated in early 2011. No changes to the UK Corporate Governance Code are planned as a result of this exercise.

Why focus on culture?
The FRC launched its culture project against a backdrop of reducing public trust in business. Mistrust of the banking sector after mis-selling scandals and the financial crisis, and corporate scandals across different sectors have called into question the integrity of some of our most respected brands. The public, the media and government are asking more questions about corporate purpose, including contribution to society, taxation and the behaviour of directors. The message that companies need to have a strong purpose, culture and ethical values to succeed and be sustainable has never been clearer.

The culture project has drawn in the views and the expertise of a number of organisations under the "Culture Coalition" banner and has involved engagement with FTSE chairmen, chief executives and company secretaries. The report "aims to stimulate thinking around the role of boards in relation to culture, and encourage boards to reflect on what they are currently doing".

Published on 20 July 2016, the report highlights the huge part culture plays in good governance and in supporting corporate purpose. It focuses on four key areas for boards to address:

- The role of the board in influencing and shaping culture
- Bringing values to life
- Building trust with stakeholders
- How boards can assess, measure and monitor culture

Feedback on the report is welcomed (to be sent to culturecoalition@frc.org.uk) and over the coming year the FRC will be monitoring reporting on culture by companies and investors.

For further information on the feedback from the FRC's culture project, please read our 'Governance in brief – FRC reinforces the importance of corporate culture'.

"A healthy corporate culture is a valuable asset, a source of competitive advantage and vital to the creation and protection of long-term value." This was a key observation from the FRC's report 'Corporate culture and the role of boards'.

In order to better drive a "healthy corporate culture", boards should be more explicit about the unifying purpose of their business and the outcomes they are seeking to generate. A well-defined business purpose links the organisation to the wider world, explicitly calling out their targeted social, environmental or broader economic role, thereby enhancing accountability, sustainability and creating greater transparency for all stakeholders.

Re-examining the duties of directors

The new Prime Minister, Theresa May, is asking serious questions about the way UK boardrooms operate and, in particular, is keen to examine the role of non-executives and the extent to which the interests of a broader range of stakeholders are considered.

Shareholder primacy is a key feature of UK company law and governance, however it was the duty to promote the success of the company for the benefit of its members as a whole (s172) which attracted much attention and debate when the Companies Act 2006 was going through the Houses over a decade ago.

There was extensive lobbying to consider a broader list of stakeholders and the result was s172 and the duty to "have regard to (amongst other matters)":

- the likely consequences of any decision in the long term;
- the interests of the company's employees;
- the need to foster the company's business relationships with suppliers, customers and others;
- the impact of the company's operations on the community and the environment;
- the desirability of the company maintaining a reputation for high standards of business conduct; and
- the need to act fairly as between the members of the company.

The FRC is encouraging companies to consider how they might report on how the directors have discharged this.

Shaping culture to drive strategy

While the execution of a business strategy can stumble for many reasons, the underlying cause is often a misalignment between strategy and corporate culture. Culture determines the habitual patterns of thinking and behaviour that shape how the strategy becomes reality. The macro business issues facing organisations today have clear cultural implications that can help or hinder strategic objectives. If a new strategy conflicts with entrenched practices, employees will struggle to change.

Culture is an enabler of business strategy

- Culture needs to be aligned with and support business strategy
- Culture change should build on current strengths, not only address gaps

Culture is shaped by leaders' actions and decisions

- Culture change must start with leaders acting as role models
- It is important to pick your battles focusing on a driving change in targeted areas

Culture is sustained by employee behaviours

- Culture must stick with most employees
- Don't try to change mindsets – change behaviours. This provides a tangible access point to drive cultural change

Culture is reinforced by business and organisational systems

- Cultural aspirations must be supported by the wider organisation architecture
- Establish a baseline and track progress with leading and lagging indicators

Assessing culture

Boards need to leverage data from within their organisation to understand themselves better – what they value, what they believe, and how they behave. Conducting a culture diagnostic, through surveys, interviews, focus groups or some other mechanism, establishes a baseline from which the board can identify the significant attributes of current culture and determine how well that aligns with current and/or future strategy.

Transforming culture

Once the desired culture is understood it may be necessary to define interventions to achieve the required cultural change. There are four major levers available to the board, with a series of interventions for each, to raise awareness of and move towards the desired change: leadership, communication & engagement, talent processes and organisations systems.

Typically organisations will start with high-level interventions from leadership, for example town hall-type events or leader role modelling. At the same time an engaging communications campaign can be launched to reinforce these messages and to set the "tone from the top".

Setting the tone from the top alone is unlikely to achieve the desired change. The tone must be reinforced at the middle and at the bottom and throughout all the various layers of supervision within the organisation. This calls for more targeted interventions in the talent and/or operations areas, for example revising the performance management approach, revising sales policies and processes and realigning the organisation structure. These changes will get people starting to experiment with the new behaviours which will drive change.

Sustaining and reinforcing culture

In order to "lock in" the desired behaviours, it is important that the board remains focused on the business purpose and outcomes and adopts an agile approach to adjusting and refining the board's intentions and culture. Boards need to continue the town hall announcements, the leader role modelling and the communication strategy, but there also needs to be emphasis on aligning other talent and organisation systems so that they continually encourage, reinforce and reward the desired behaviours.

"If left to its own devices, [culture] shapes itself, with the inherent risk that behaviours will not be those desired".

Boards must make the time, and develop the mechanisms, to continually monitor and nurture the organisation's culture if they want to generate and protect longer-term value and drive a unified business purpose.

Contacts – Deloitte Culture Solutions

Deloitte's CulturePath™ solution can deliver compelling and actionable visibility into an organisation, progressively guiding the organisation throughout its business journey and giving it confidence to lead the way forward.

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Audit committee – focus on internal controls

The UK Corporate Governance Code makes the board accountable for Risk Management and Internal Controls. More precisely, the board needs to review the effectiveness of the internal controls, financial, operational and compliance controls, and report on them.

To meet these requirements organisations have spent significant time and effort focusing on strengthening their risk assessment and disclosure process. Whilst this is a positive step, audit committees should ensure that equal efforts are being allocated to assessing internal controls frameworks.

A continuous journey

The new emphasis in the code on "ongoing monitoring" of the risk management and internal control systems reflects the dynamic nature of these systems and the need to regularly review and assess risks and internal controls. In short, there is a continuing journey to go on.

In order to assess whether the controls continue to be fit for purpose, audit committees need to ensure that processes and information are in place to answer the following key questions:

- Have all material controls been identified appropriately?
- Do monitoring processes and risk indicators at board level cover all principal risks and material controls?
- Are necessary actions being taken promptly to identify the root causes and remedy any significant control failings or weaknesses?
- Do the auditors rely on our controls and if not, why not?
- Where are the sources of assurance on control effectiveness and are they sufficient?

The Board should monitor the company's risk management and internal controls systems and, at least annually, carry out a review of their effectiveness and report on that review in the annual report. The monitoring and review should cover all material controls including financial, operational and compliance controls.

To support the board, the audit committee needs to obtain and review a comprehensive mapping of the existing assurance framework around principal risks and material controls. And material controls need to cover financial controls, operational controls as well as compliance controls.

Effective controls

We sometimes find that employees across organisations feel that controls are not adding any value to the business, controls are not cost effective, sometimes not efficient and are not an integral part of the day to day business. They are there only to tick the compliance box. However, considering the controls framework with fresh eyes can unlock efficiency and cost savings in addition to complying with regulations. Our work with a number of organisations has identified significant opportunities for organisations to maximise controls automation; rationalise and standardise controls for better alignment with business requirements, and build a cost effective centralised controls monitoring framework.

Optimising a Controls Framework follows four key principles: Automate, Align, Simplify and Standardise.

- **Automate:**
  Organisations need to leverage their existing ERP framework and maximise use of in-built configuration controls. Configuration controls are one of the key components of automation and help build strong 'automated-preventive' controls. As part of controls automation organisations need to focus on data validation, data integrity, data classifications, access and segregation of duties, interfaces and automated monitoring through analytical tools.

The range and quality of governance, risk and compliance (GRC) tools available has increased significantly in recent years. We find that minimising reliance on excel spreadsheets and uncontrollable manual processes strengthens the Board's confidence in the effectiveness of internal controls.

- **Align:**
  Aligning controls to the risk appetite, business objectives, values and value drivers of the organisations will support enhancement of business performance and promote acceptance and ownership of the controls framework across the organisation.

- **Simplify:**
  Organisations need to rationalise the number of controls. With maturing and improving business processes, companies should challenge existing manual controls and focus on fewer but better designed controls. They are easier to communicate and embed across the organisation.

- **Standardise:**
  A balanced approach to having standardised global controls objectives with flexible local control activities (but within global minimum standards) will help to build a robust controls framework across the organisation. Organisations need to leverage shared service centres to help enforce standardisation and monitoring of material controls. This will also help to build a cost effective centralised controls operating model that ensures effective operations and efficient monitoring of controls.

Next Generation Controls		
	Transparency	**Clear linkage** between processes, the associated risks, and the controls to mitigate that risk
	Simplicity	**A clear, easy to** understand risk and control **framework**
	Efficiency	**Lower cost** (internal and external) of **operating and assuring controls**
	Effectiveness	Protect reputation through **improved quality and consistency** of control operation across markets
	Sustainability	**Easier to maintain and govern** risk and control activities
	Flexibility	**Easier to adapt** for future business change

Reporting on internal controls is a way of communicating the quality of those controls to the market. With the changes to risk management and internal control disclosures arising from the 2014 Code, in some cases the disclosure required by DTR 7.2.5R of the main features of the company's internal control and risk management systems in relation to the financial reporting process has been omitted from more recent annual reports. This is ordinarily included in the audit committee report – it is worth checking that it has not fallen off your reporting radar.

Key questions for consideration

- Do you have a robust controls environment that supports growth and better business performance?
- Do you understand what IT controls you already have? Have you maximised controls automation or is it still manual and Excel spreadsheet dependent?
- Do you have a mature shared service centre? Have you considered delivering your risks, controls and compliance activities through the shared service centre?
- What is the cost of your controls operations and monitoring? Can standardisation and automation help you achieve significant cost reductions while strengthening internal controls?

Contacts – Risk Advisory

Deloitte's Risk Advisory team works with clients to help them manage risk and create value. The team works collaboratively with client organisations to either assess existing processes in place or to assist in the implementation of pragmatic risk solutions.

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Getting the most from your internal audit function

Background

The FRC's recent updates to the UK Corporate Governance Code, as well as to its Guidance on Audit Committees, took effect for financial years commencing on or after 17 June 2016. The updates are 'light touch' with respect to Internal Audit and, in our opinion, reflect existing good practice. Included in the guidance are two explicit requirements to:

- **assess the effectiveness of the Internal Audit function annually; and**
- **consider the need for an external independent review, also on an annual basis.**

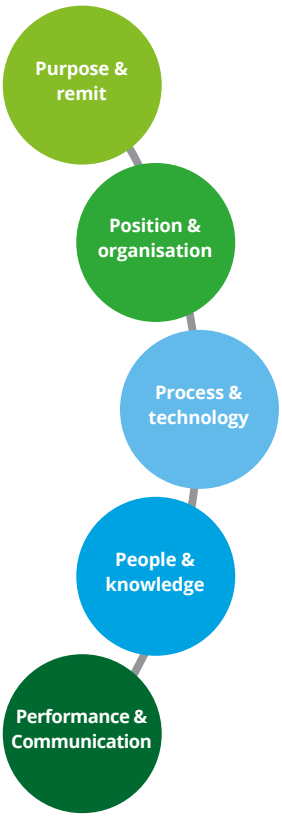
Given the increased focus on Internal Audit effectiveness, here are our perspectives on what makes a good Internal Audit function and some practical tips on how its effectiveness can be assessed.

It is not unusual for us to hear comments such as: "Internal Audit don't understand the business"; "We only talk to Internal Audit during audits"; or "Internal Audit focus on the risks that don't really matter". Comments of this nature reinforce the fact that even if a function has clear processes, and is efficient in delivering its audit plan, it may not be **effective in the eyes of those receiving the service**. Lack of business understanding, poor relationship management and lack of relevance can severely damage the impact and value that Internal Audit bring to its organisation.

Good Internal Audit functions have a broad remit, mirroring the variety and complexity of their organisation and the risks that are faced. They keep abreast of business issues, changes and risks, translating them into a relevant audit plan.

For example, leading Internal Audit functions may be involved in organisational change programmes and process improvement projects, providing early feedback on the design of management's proposed controls, allowing the function to stay close to the business. Furthermore good functions have overcome the traditional skills challenge and are able to bring the right expertise to the right audits. For example, they effectively leverage guest auditors, rotational talent programmes, third party specialists and second line function expertise.
Good Internal Audit functions also actively build and maintain strong relationships with management. This includes having regular interactions outside of specific audit work, providing insight into functional areas and helping share good practice across their organisations.

Attributes of a good Internal Audit function



Key attributes of an effective Internal Audit function that we consider during our independent effectiveness reviews include whether the Internal Audit function:

- is seen as a business partner and is actively approached by the business for assurance support;
- is an effective challenger to and adviser of the risk management process;
- has a clear identity, brand and focus with respect to its role and remit;
- provides insights on emerging risks, thematic observations and holistic issues;
- is seen to be an objective assurance function which is appropriately independent of management and free from operational responsibility;
- is an effective enabler of change evidenced by high take up and implementation of audit recommendations;
- interfaces effectively with other assurance providers, applying procedures to gain an overview of assurance activity and ensuring that the work is carried out to a suitable standard, which can be relied upon;
- uses data analytics to inform annual planning and risk based auditing, with a focus on root cause analysis and process improvement; and
- provides a clear and succinct picture of the through engaging reports that focus on the things that matter most.

Monitoring the effectiveness of Internal Audit

Monitoring the effectiveness of Internal Audit is often reliant on a combination of viewpoints from sources with varying degrees of independence from Internal Audit. Typically these include:

- **Internal Audit's self-assessment** – Head of Internal Audit led review, including review of data on performance against Key Performance Indicators, summary of feedback from post-audit questionnaires and key stakeholder interviews.
- **The audit committee's assessment** – The audit committee chair would review and challenge Internal Audit's self-assessment, and supplement this with, for example, additional stakeholder interviews; consider coordination of assurance providers; consider the uptake of audit recommendations and impact of the internal audit function.
- **An independent third-party's opinion** – Independent reviews provide a formal, impartial opinion on the effectiveness of the Internal Audit function. They include stakeholder interviews, desktop reviews of processes, methodologies, sample audit files and sample reports, as well as benchmarking the function against similar functions in the same industry.

Industry insight: The Chartered Institute of Internal Auditors has recently published a revised set of standards which are effective from 1st January 2017. The revision introduces two new standards aimed at formalising expected good practice around safeguards to independence, and a number of amendments to existing standards that could impact on current working practices.

Deloitte View

- The FRC only requires an independent, third party review of Internal Audit effectiveness to be **considered** on an annual basis, whereas existing Institute of Internal Auditors Standards recommend that this is actually performed at least every five years.
- In our experience, Internal Audit effectiveness reviews provide the greatest benefits and insight where there has been a key change in the function, stakeholders or business. For example, we typically see independent Internal Audit effectiveness reviews requested when there has been a change in:
  - the Head of Internal Audit;
  - the business and/or corresponding Internal Audit strategy;
  - Internal Audit working practices; or
  - audit committee members.
- Given the pace of change within risk and internal audit, independent effectiveness reviews invariably identify opportunities for Internal Audit functions to improve.

As an Audit Committee member, do I...	Does our Internal Audit function...
• Understand and agree with Internal Audit's strategy, purpose and remit? • Feel Internal Audit have sufficient understanding of the business' strategy and risk environment? • Understand the company's Assurance Map? • Understand what assurance can be provided by Internal Audit? • Understand how the sources of assurance e.g. management (2nd line of defence) and other assurance providers (3rd line of defence) contribute to the overall assurance map? • Assess whether Internal Audit's work is sufficient and aligned to principal risks? • Have confidence that Internal Audit is independent and free from management influence? • See effective working relationships between internal Audit and management? • Monitor the Internal Audit function's performance against its strategy? • Know when the last independent effectiveness review was performed?	• Have a clear charter outlining its role, remit and position in the organisation? • Have a clear defined methodology and robust quality assurance process? • Have the right profile and leadership to deliver on their mandate? • Have sufficient skills and knowledge, and make use of specialist expertise to support technical/complex risk areas e.g. Cyber Security, operational risk? • Leverage analytics to provide business insights and trends? • Complete their Audit Plan to time and on budget? • Produce high quality reports that get to the point and focus on the areas which matter? • Provide management and the audit committee with insights on emerging and external risks? • Have knowledge sharing mechanisms to join the dots for management between good practice seen in different areas of the business?

Contacts – Internal Audit

Our internal audit practice specialises in providing internal audit effectiveness reviews as well as delivering outsourced or co-sourced internal audit services.

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Modern Slavery Act 2015

Deloitte.

March 2016

Governance *in brief*
Modern Slavery Act 2015

Headlines

- The Modern Slavery Act was published on 26 March 2015.
- All organisations with UK operations and turnover in excess of £36 million, with a year end on or after 31 March 2016 are required to publish a slavery and human trafficking statement on their website as soon as reasonably practicable after the year end.
- This statement must set out the steps that an organisation has taken during the financial year to ensure that no slavery or human trafficking is taking place within the organisation or its supply chains, including all third party suppliers and subcontractors.
- The extreme case of modern slavery is not the only area of labour exploitation that is coming under increased focus by BIS and by governments around the world.

Background

The Modern Slavery Act 2015 ("the Act") was published in March 2015, in response to heightened concern around slavery, human trafficking and forced labour in global supply chains and recognises the role that companies can play in tackling these crimes.

Deloitte has been involved with the Act since before its publication, including working with the Home Office and US State Department to bring together leaders from government, the private sector and NGOs to share ideas on tackling modern slavery. We consider the Act an important step to raise awareness of modern slavery and labour exploitation and believe that all reputable organisations should embrace its requirements.

What is modern slavery?

Modern slavery is a broad term for the criminal activity for certain aspects of the abuse of human rights. It includes the offences of slavery, servitude and forced or compulsory labour, as well as human trafficking.

Slavery: The key element of slavery is the deprivation of freedom and behaviour on the part of the offender as if they own the victim.

Servitude: Forcing an individual to provide services through the use of coercion. This includes the obligation for the victim to live on another person's property and being unable to change this condition.

Forced or Compulsory Labour: Work or service is obtained from an individual under the menace of any penalty. They have not offered this work or service voluntarily.

Human Trafficking: The offender arranges or facilitates the travel of the victim with a view to that person being exploited – this can be even where the victim consents to the travel, as they may have been deceived or unduly influenced.

In 2015, the International Labour Organisation (ILO), an agency of the United Nations, estimated that 21 million people are victims of forced labour around the world, generating approximately US$150 billion a year in illicit profits. The Modern Slavery Act provisions are designed to encourage businesses to tackle modern slavery head on.

The Deloitte Academy

The Business & Human Rights Resource Centre is currently maintaining a public track record of companies' reporting under Section 54 of the Modern Slavery Act 2015.

For years ending on or after 31 March 2016, all organisations with total global annual turnover exceeding £36 million that are conducting business anywhere in the UK must produce a slavery and human trafficking statement for each financial year. December reporters will be required to report for the first time following their 31 December 2016 year end.

The Act does not specify the content and structure of the statement, the only strict requirements are that it must:

- detail all the steps taken during the financial year to ensure that slavery and human trafficking are not taking place in any of the company's supply chains or any part of the business (or make a negative statement that the organisation has taken no such steps);
- be approved by the board of directors and signed by a director (or equivalent); and
- be published on the organisation's website and include a link to the slavery and human trafficking statement in a prominent place on that website's homepage.

It is up to individual companies to determine the content and level of detail to disclose.

Although the risk resides in the supply chain, it will require central oversight given its nature and the reputational risk, and therefore we consider it should be added to the board's compliance or risk register so that the board receives appropriate regular updates.

The Business & Human Rights Resource Centre is currently maintaining a public track record of companies' reporting under Section 54 of the Modern Slavery Act 2015. This can be accessed via: https://business-humanrights.org/en/uk-modern-slavery-act-registry.

We encourage companies to look at a selection of their peers and competitors to identify good practice which could be emulated in their own reporting.

Contacts – Sustainability and modern slavery

Deloitte's sustainability and modern slavery assurance and advisory team provides assistance to clients on modern slavery, including policy and strategy development, risk assessment and supplier engagement, through to disclosure, advisory and assurance services.

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Gender Pay Gap reporting

Deloitte.

March 2016

Governance *in brief*
Gender pay gap information
– draft regulations issued

Headlines

- Draft regulations call for pay and bonus information across genders to be reported publicly by all employers with 250 or more relevant employees.
- New analysis of pay information will help employers understand the extent of any gender pay gap in their organisation.
- It is proposed that the first data should be collated as at 30 April 2017, just one year away, and reported within twelve months of that date.

Background

The government believes that employers are losing out by not effectively utilising women's academic achievements, experience and talents. It is hoped that increasing transparency around gender pay differences will enable the impact of workplace policies and practices promoting gender equality to be monitored and remedial action to be prioritised.

Tackling the gender pay gap is a key priority for the current government. The Prime Minister has made clear the government's ambition to eliminate the gender pay gap in a generation, and the Government Equalities Office has now published draft regulations, along with its response to the '*Closing the Gap*' consultation on gender pay disparity which closed in September 2015. Interested parties were invited to provide comments by 11 March 2016. The government intends to lay the regulations before Parliament over the summer.

The headline requirements

Employers are being asked to publish the following information for each financial year:

- the percentage difference in **mean** pay between male and female employees;
- the percentage difference in **median** pay between male and female employees;
- the percentage difference in the **average bonuses** received by male and female employees;
- the proportion of men and women who receive **bonuses**; and
- the number of men and women in each **quartile of pay** within the workforce.

Which companies will be caught by the new regulations?

Employers with 250 or more relevant employees will fall within the scope of the regulations. A relevant employee means someone who ordinarily works in Great Britain and whose contract is governed by UK legislation.

The Deloitte Academy

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Employers with 250 or more relevant employees will fall within the scope of the regulations, which have not yet been laid but are still expected to commence in the coming months, with the first "snapshot" of information taken in April 2017 for publication by April 2018. A relevant employee means someone who ordinarily works in Great Britain and whose contract is governed by UK legislation.

Employers are being asked to publish the following information for each financial year:

- the percentage difference in mean pay between male and female employees;
- the percentage difference in median pay between male and female employees;
- the percentage difference in the average bonuses received by male and female employees;
- the proportion of men and women who receive bonuses; and
- the number of men and women in each quartile of pay within the workforce.

The Government also expects that employers will want to provide additional narrative that provides context, explanation for pay gaps and sets out what actions will be taken. This will be strongly encouraged within the guidance accompanying the regulations.

The draft regulations and the behavioural change that the transparency will encourage are important steps in achieving greater gender parity, for pay and representation, at all levels within larger businesses. This new legislation will stimulate companies to review their reward strategies.

For many companies, this will be quite some work, and this will emphasise the importance of good data within HR and payroll systems.

Contacts – Human Capital

Deloitte's market leading Human Capital practice advises on reward strategy, organisation design, systems evaluation and implementation.

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Timeline of key changes in corporate governance

Applies	What?	Applicable to	Notes
31 March 2016	The Modern Slavery Act 2015	Applicable to commercial organisations supplying goods or services, in any sector, with a total turnover exceeding £36 million, conducting business anywhere in the UK.	Applies to periods ending on or after 31 March 2016.
17 June 2016	New EU Audit Regulation and 2016 UK Corporate Governance Code and a revised Guidance on Audit Committees	Applies to all companies with a Premium listing of equity shares regardless of whether they are incorporated in UK or elsewhere.	Applies to periods commencing on or after 17 June 2016.
3 July 2016	ESMA Guidelines on Alternative Performance Measures (APMs)	ESMA guidelines apply to APMs disclosed in regulated information by issuers in the EU with securities traded on regulated markets and prospectuses.	The ESMA Guidelines are effective for relevant documents issued on or after 3 July 2016, regardless of the accounting period.
15 September 2016	Publication of UK tax strategy (Finance Act 2016)	Applicable to multinational businesses with UK operations and turnover in excess of €750 million, or UK registered companies, partnerships and permanent establishments with turnover in excess £200 million or gross assets in excess of £2 billion.	Applies to periods commencing on or after 15 September 2016.
5 April 2017	Gender Pay Gap Reporting	Applicable to employers of 250 or more relevant employees. A relevant employee means someone who ordinarily works in Great Britain and whose contract is governed by UK legislation.	Regulations are not yet final, but we expect the first data collection point to be 5 April 2017.
25 May 2018	General Data Protection Regulation	Applicable to organisations that process EU citizen data, even if they have no legal presence in the EU.	Enforced from 25 May 2018.
17 June 2019	70% cap on non – audit services fees for Public Interest Entities	Applicable to EEA Public Interest Entities (PIEs). A PIE is a public interest entity, defined in EU law as being an entity governed by Member State law with securities (debt or equity) admitted to trading on an EEA regulated market (including LSE Premium or Standard Listing, not AIM), a credit institution, (bank or building society in UK terms) or insurance undertaking.	Applicable to periods commencing on or after 17 June 2019, unless there has been a change of auditors, in which case it applies in the fourth year of engagement for the new auditors.

Further resources

Throughout this publication we have mentioned some of our other publications where they offer a deeper dive on the governance topics of interest, or where we believe they can add insight to your role as an audit committee member. We have also created checklists to assist you in discussing these matters with your companies.

This section pulls together those additional resources with a brief introduction to each of them, so they are easier to refer to.

As always, do get in touch with your Deloitte partner or with us in the Deloitte governance team if you would like to discuss any areas in more detail. All our governance publications are available to read and download from www.deloitte.co.uk/governancelibrary.

Governance *in brief*

Cyber risk – how are boards responding? explores the results of the third annual FTSE 350 UK Cyber Governance Health Check run by UK government and provides insights into how boards are strategically managing and responding to cyber risk.

FRC reinforces the importance of corporate culture explores the role of the board in influencing and shaping culture and the need for improvement in reporting on culture in the annual report.

Publication of your UK tax strategy identifies key considerations and implications of revised legislation on tax transparency (2016 Finance Bill), which requires large businesses within its scope to publish their tax strategy in relation to UK taxation on their website before their financial year end.

The vote to leave – key considerations for half year reporting explores the implications of the EU referendum result and identifies key considerations for audit committees – implications to corporate reporting, external audit, status of EU reporting and audit requirements, direct and indirect tax implications.

For further information on the EU Referendum results, we have a dedicated webpage www.deloitte.co.uk/eu-referendum.

EU Privacy Legislation explores the recent issues with transfer of data between the EU and the US and the existing solutions, the EU General Data Protection Regulation (GDPR) which is set to be enforced from 25 May 2018, and includes a series of questions to consider when determining how well prepared your organisation is for the upcoming changes.

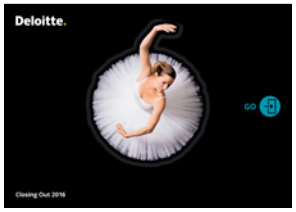
FRC issues 2016 UK Corporate Governance Code, Guidance on audit committees and changes to auditor independence rules identifies and explores key changes arising from the FRC's 2016 updates to the UK Corporate Governance Code, the Guidance on Audit Committees and to standards for auditors. We highlight areas for directors to consider when approaching their first year of reporting under the 2016 UK Corporate Governance Code.

Risk, internal control and longer-term viability – unlocking the value identifies and explores some of the benefits we have seen for companies from implementing the new longer term viability statement, providing companies with areas to consider in order to ensure they are deriving the most value from this exercise as they approach their second year of reporting under the new requirements.

Gender pay gap information – draft regulations issued explores the draft regulations issued to tackle the gender pay gap. The Prime Minister has made clear the government's ambition to eliminate the gender pay gap in a generation, and the Government Equalities Office has now published draft regulations. Employers with 250 or more relevant employees are being asked to publish detailed gender pay information on their website for each financial year.

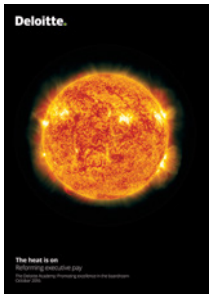
Modern Slavery Act 2015 explores the background to the Modern Slavery Act 2015, the reporting requirements, including which companies must comply, and suggests some areas for organisations to consider when preparing to issue their first modern slavery and human trafficking statement, including adding the requirements to the board's central compliance register or risk register.

A clear vision: Annual report insights 2016 gives a comprehensive picture of narrative and financial reporting trends for UK listed companies, together with ideas to help them improve their annual reports.

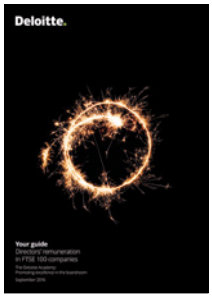


Closing Out 2016 discusses the principal financial reporting issues arising in respect of 31 December 2016 annual reports, covering areas of regulatory focus identified in the FRC's Annual Review of Corporate Reporting 2015/2016, ESMA's enforcement priorities and issues arising from the current economic environment and developments in reporting standards.

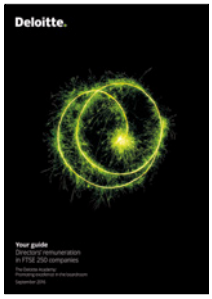
Other recommended publications



The heat is on: Reforming executive pay discusses the key aspects of current focus on executive pay and explores the possibilities of possible solutions.



Your guide: Directors remuneration in FTSE 100 companies presents analysis and insights regarding executive directors' remuneration in FTSE 100 companies, based on the 2016 reporting and AGM season.



Your guide: Directors' remuneration in FTSE 250 companies presents analysis and insights regarding executive directors' remuneration in FTSE 250, based on the 2016 reporting and AGM season.

Risk appetite: Is your disclosure where you want it? presents a pragmatic, multi-stage approach to risk management and determining risk appetite, outlining the key content for each stage and concluding with a range of key questions for boards to consider.

Reputation matters: Developing reputational resilience ahead of your crisis identifies two fundamentals in building reputational resilience – identification of risks from an outside in perspective, and being prepared for a crisis through a robust crisis readiness programme. Looking ahead, it will be the organisations that understand, protect and develop their reputation asset that will be best placed to maintain shareholder value.

Key areas of focus for this year end and beyond

Checklist for reviewers of the audit committee report

The audit committee is responsible for providing an independent level of oversight of public reporting on behalf of shareholders and to ensure their interests are protected in respect of financial reporting and internal control. This includes but is not limited to the annual report. We recommend that wherever possible the audit committee report should explain the level and nature of challenge posed to management by the audit committee during the year.

The checklist is drawn from a number of sources. The key below indicates whether a disclosure is from the UK Corporate Governance Code, recommended by the FRC's Guidance on Audit Committees, a feature in a report from the FRC's Financial Reporting Lab, an area of focus identified by the FRC in other recent publications (for instance, the CRR's report in October) or our recommendation for good practice.

Checklist contents

1. Introduction by the chairman
2. Audit committee composition
3. Role and responsibilities
4. Meetings
5. Performance evaluation
6. Interaction with the board and board committees
7. Fair, balanced and understandable – including key areas of focus relating to the strategic report
8. Longer term viability statement
9. Significant issues affecting financial reporting – including key areas of focus relating to the financial statements
10. Risk management and internal control
11. Internal audit
12. External audit: audit tendering and rotation
13. External audit: fees and non-audit services
14. Effectiveness of the external audit process
15. Interaction with regulators
16. Additional considerations for FTSE 350 companies

	Content requirement/recommendation	Your comments and notes
1.	**Introduction by the chairman**	
1.1 L R	Introduction or comment by the audit committee chairman to: • show ownership of the contents of the report; • highlight key matters; and • flag any changes during the year.	
1.2 R	The audit committee chairman should explain their personal experience of how the audit committee achieved its objectives during the year and any observations on the future work of the committee.	
1.3 L	Other ways to personalise the report might include using a photograph of the audit committee chairman or the audit committee chairman signing the report.	

Key:

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	Content requirement/recommendation	Your comments and notes
2.	**Audit committee composition**	
2.1 G	The names and qualifications of all members of the audit committee during the period. *Note: When considering the requirements for reporting on composition of the audit committee, a cross reference to the directors' biographies page of the annual report could avoid the need to repeat lengthy details about members' experience.* *There should be at least three or, in the case of companies below the FTSE 350, two members.These should be independent non-executive directors.*	
2.2 G	Identification of those deemed to be the member(s) with recent and relevant financial experience. *The DTR indicates that at least one member must have competence in accounting or auditing, or both, for periods commencing on or after 17 June 2016.*	
2.3 G	Explain how the audit committee as a whole meets the provision to have competence relevant to the sector in which the company operates. *A new requirement for periods commencing on or after 17 June 2016, although some will choose to include this explanation in earlier reports.*	
2.4 G	Provide any additional detail required to demonstrate how the audit committee composition requirements have been addressed.	
2.5 R	Details of any changes in the composition of the audit committee during the year, together with reasons where appropriate and any relevant cross-references. It is useful to readers to be clear about changes in membership and why any new members joined the committee.	
3.	**Role and responsibilities**	
3.1 C	Summary of the role and responsibilities of the audit committee during the year. *Note: We recommend including words that capture the overall mission, preferably in the words of the audit committee chairman, based on his/her own experience of fulfilling the role, i.e. what does the audit committee believe it is there to do.* *This could be included in the audit committee chairman's introduction.* *It should be clear that the audit committee acknowledges and embraces its role of protecting the interests of shareholders as regards the integrity of published financial information by the company and the effectiveness of audit.*	

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	Content requirement/recommendation	Your comments and notes
3.2 R	The audit committee could also explain its role in relation to the front half of the financial statements and their review of the "fair, balanced and understandable" and "sufficiency of information" statements by the board (either here or in the 'interaction with the board' section).	
3.3 R	Details of any changes to the role and responsibilities of the audit committee during the year.	
3.4 R	The role of the audit committee ordinarily also includes a broader remit regarding the integrity of communications with the market, analyst presentations and announcements. When describing this, the audit committee could also describe responsibilities for new forms of reporting outside the annual report, for example the Modern Slavery Act 2015 statement. *Other disclosures outside the annual report might include gender pay gap reporting, for which the first "snapshot" will need to be taken in April 2017 and, for the largest companies, UK tax strategy reporting.*	
4.	**Meetings**	
4.1 G	The number of audit committee meetings held during the year.	
4.2 R	It is useful for readers to understand the content covered in these meetings, the extent to which this was different to the 'norm' (both in terms of frequency and attendees) and how the timing of meetings was designed to fit with the overall financial reporting timetable.	
4.3 R	It is also useful for readers to understand whether other individuals are regularly invited to audit committee meetings. These may include the CFO, other board members, the Head of Internal Audit and the external auditor.	
4.4 R	Alongside these disclosures it is usual to disclose whether the audit committee has held a separate meeting, or part of meeting, with the external auditor without management being present. Some audit committees make similar disclosures regarding private meetings with the internal auditor.	
4.5 G R	"The committee should consider the clarity of its reporting and be prepared to meet investors." Either the introduction, a dedicated investors section or this meetings section of the audit committee report represents an opportunity to describe the committee's availability for such meetings and whether any have taken place during the period.	

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	Content requirement/recommendation	Your comments and notes
5.	**Performance evaluation**	
5.1 G	Provide details of how the performance evaluation of the audit committee has been conducted.	
5.2 R	Whilst this may be achieved through clear and explicit cross-reference to the board performance evaluation description in the main body of the corporate governance statement or in the nomination committee report, it will usually be appropriate to record any significant findings of performance evaluation and identify the future actions the audit committee intends to take to remediate those findings in the audit committee report itself.	
5.3 R	It is useful for readers to understand the actions taken by the committee to address any findings of the prior year's performance evaluation.	
6.	**Interaction with the board and board committees**	
6.1 R	Details of any interactions with other board committees, for example shared responsibilities relating to risk management, plus relevant cross-references.	
6.2 R	If there have been areas of unresolved disagreement between the audit committee and the full board, consider reporting on the issue. *Note: Certain areas of disagreement, for example relating to appointment of the external auditor, are required disclosure. Other areas of disagreement should be considered.*	
7.	**Fair, balanced and understandable**	
7.1 R	If the audit committee has been asked to advise the board on the fair, balanced and understandable assertion, some detail of the work performed to provide that advice, plus relevant cross-references.	
7.2	Areas to focus on when considering and preparing disclosure regarding the fair, balanced and understandable statement required by the UK Corporate Governance Code in respect of the annual report as a whole:	

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	Content requirement/recommendation	Your comments and notes
F L	• Strategic report. Have you considered whether the information in the strategic report is balanced and comprehensive (a legal requirement for strategic reports)? Is it sufficiently clear and concise? • Business model: – Is there a clear explanation of how the company creates value and what differentiates it from its peers? – Have the findings of the Financial Reporting Lab's report on the business model been reviewed and considered for implementation? – Is there sufficient company-specific and year-specific information on the business, its environment and the risks it faces? • Alternative Performance Measures (APMs): Have you assessed whether the use of APMs inappropriately replaces or obscures IFRS or UK GAAP measures?	
F R	• Does the strategic report cover both positive and negative aspects of performance and developments? *Note: Some leading companies receive a report from management that lists good and bad news during the period, so that the audit committee can assess whether the balance is appropriate.*	
F R	• Is there clear linkage between information such as strategic objectives, KPIs and risks? • Is there clear linkage between discussions of performance, position and cash flows and the financial statements? • What about the linkage between strategy, performance and remuneration?	
F	• Has management removed all immaterial items?	
F	• If the board has chosen to report on how directors have discharged their duties to have regard to other stakeholders, as outlined by section 172 of the Companies Act 2006, it will be important to consider whether this disclosure is fair, balanced and understandable.	

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	Content requirement/recommendation	Your comments and notes
8.	**Longer term viability statement**	
8.1 R	If the audit committee has been asked to advise the board on the robust assessment of principal risks and/or the longer term viability statement, disclose some detail of the work performed to provide that advice, including challenging the robustness of forecasts (also see 9.1) plus relevant cross-references. *Note: If there are concerns over the robustness of forecasting or the quality of work performed for the longer term viability statement, the audit committee should consider whether this also impacts management's conclusion on going concern.*	
8.2 F	Are you satisfied with the quality of the rationale behind the lookout period used for the longer term viability statement and with the explanation included in the annual report?	
8.3 R	Have you considered a broad range of factors when determining the principal risks and uncertainties facing the business (for example cyber security and climate change)? Have you considered how solvency, liquidity or other principal risks affect the long-term viability of the business? What qualifications and assumptions were made and have you considered whether any of those should be disclosed? How was the underlying analysis performed? Were principal risks considered only individually or also in combination?	
9.	**Significant issues affecting financial reporting**	
9.1 R F	The audit committee's challenge of the robustness of management forecasts underlies both the assessment of longer term viability (above) and many of the significant judgements affecting financial reporting. The pervasive nature of forecasting means they underpin numerous areas of the financial statements, from asset valuations to taxation.	
9.2 L	It is useful for the audit committee to compare the significant issues from this year to those from the prior year, explaining where and why changes have arisen, or stating that there are no changes. Some audit committees separate significant issues between recurring and one-off issues.	
9.3 G F	Including a brief summary of the nature of the significant issue can make it clear to the reader why the issue was deemed to be important to this specific company in that particular reporting year. *Note: A cross reference to where the issue is discussed elsewhere in the annual report is recommended to avoid repetition where possible.*	

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9.4 R	How the audit committee reached a position that it was satisfied with the treatment adopted by management. The audit committee should explain the conclusion they have reached and the rationale for how they reached that conclusion, including some detail of the information they have looked at and where it was sourced, the extent to which the discussions arising led to a change in treatment.	
9.5 L R	We also recommend that the issue includes quantification and any relevant cross-references, where appropriate (references to other relevant parts of the annual report, for example principal risks or the notes to the financial statements, particularly the disclosure on critical accounting judgements and key sources of estimation uncertainty).	
9.6 R	Audit committees may wish to discuss the interactions with the external auditor on each issue. Consider whether to add further detail relating to items communicated by the auditor – some audit committees now include detail on misstatements identified by the auditor and whether they have been corrected.	
9.7	Other areas audit committees may wish to consider disclosing when assessing significant issues and reviewing the annual report:	
F	• UK referendum result – has management: – Considered the consequential risks and uncertainties in the political and economic environment and the impact of those risks and uncertainties to your business? – Determined what disclosures, if any, are required to meet the needs of investors and comply with regulatory requirements? – Ensured that disclosures are company specific with any anticipated effects quantified?	
F	• Tax transparency – has the annual report: – Explained the factors affecting the effective tax rates and their sustainability (or expected variation?) – Clearly articulated how you account for material tax uncertainties by explaining the basis for recognition and measurement? – Disclosed the amount of tax provisions? – Disclosed which estimates and judgements are relevant to the context? – Responded to increased stakeholder scrutiny of tax strategies, including the jurisdictions in which you pay tax? – Clearly described any material risks to which the need for increase in tax transparency gives rise?	

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F	• Dividends – has the annual report disclosed how dividend policies operate in practice linked to how those policies may be impacted by the risks and capital management decisions facing the company? • Has the board concluded on whether the company is going to disclose the level of distributable reserves?	
F	• Low interest rates – have management and the audit committee: – Considered the impact of low interest rates on the amounts currently reported in the financial statements? – Considered the valuation of long term assets and liabilities (e.g. the effects of adjusted discount rates on pension scheme liabilities and suppressed returns on pension scheme assets)? – Included sensitivity analysis within the annual report to highlight the potential impacts?	
F	• Critical judgments and estimates – does the annual report: – Clearly explain the specific judgements the board has made and their effect on the financial statements? – Include any quantitative disclosures, such as sensitivities or ranges of outcomes, that would help the users of the accounts to fully understand the potential effect of estimates, including the effects on the following year? *Note: The FRC wants to see companies quantifying and disclosing ranges of outcomes and how potential changes could affect the next financial year.*	
F	• Accounting policies: – Has management considered improvements in the disclosure of accounting policies, particularly in relation to revenue recognition? – Is there specific, granular policy information and clear link between the sources of income and divisional structure described in the business model and revenue recognition policies? – Does the annual report explain when exactly the revenue from complex long term contracts is measured?	
F	• Pension reporting: – Do pension disclosures adequately explain the risks to which the company is exposed by the pension plan? – Does the disclosure of the plan's assets clearly reflect the nature of the plan's investments? *For example, this might include an explanation of the methodology used to estimate fair values for complex financial instruments such as insurance contracts.*	

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R	• Have you considered the completeness and clarity of the disclosures in relation to cyber risk – and is cyber risk sufficiently high on the risk register and given sufficient focus at audit committee meetings?	
R	• Have you considered the latest developments with regards to the EU General Data Protection Regulation and how well prepared your organisation is for the upcoming changes – are any amendments needed to your risk register or audit committee reporting?	
F	• Have you considered the need for disclosures regarding the major IFRS standards that will become effective in the near future in particular IFRS 15 *Revenue from Contracts with Customers*, IFRS 9 *Financial Instruments* and IFRS 16 *Leases*. *Note: Comparative periods for IFRS 15 and IFRS 9 will commence 1 January 2017 so companies should be able to report with real clarity at this stage.*	
10.	**Risk management and internal control**	
10.1 G	Include a description of the audit committee's oversight role regarding the risk management and internal control systems – this could explain the split of duties between the board, the audit committee and any other board committees with responsibilities in this area. *Note: The board has overall responsibility for an organisation's approach to risk management and internal control but may delegate certain functions to the audit committee. The audit committee is expected to have oversight of the company's internal financial controls.*	
10.2 G R	The audit committee should review and recommend to the board the disclosures in relation to internal control and risk management unless this is dealt with by the board or another board committee – the board may wish to describe the work they have performed to understand the material controls in place, review the systems of risk management and internal control, and validate the related disclosures.	
10.3 R	Provide details of any significant changes in risk management and internal control systems during the year. This could be achieved through a cross-reference to another part of the annual report.	
10.4 DTR	Describe the main features of the company's internal control and risk management systems in relation to the financial reporting process and the process for preparing consolidated accounts. *These disclosures required by DTR 7.2.5R and DTR 7.2.10R are often found in the audit committee report; the requirement is to include the disclosures in the corporate governance statement.*	
10.5 R	Explain how the audit committee has ensured management has responded to or followed up on any issues identified.	

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11.	**Internal audit**	
11.1 R	Explain the audit committee's involvement in the development and approval of the internal audit plan. If principal risks to the business have been taken into account when developing the internal audit plan, it is worth saying so.	
11.2 R	Where appropriate, emphasise internal audit's risk focus and reflect that the programme is regularly updated in accordance with the changing risk profile of the company.	
11.3 G	Explain the role of the audit committee supervising the result of internal audit's work.	
11.4 G R	Explain how the audit committee assessed the effectiveness of internal audit and provide relevant detail around whether internal audit has sufficient quality, experience and expertise, including the head of internal audit, particularly where there has been a change in the head of internal audit.	
11.5 R	Explain the reporting channels for internal audit.	
11.6 R	Explain how the audit committee has ensured management has responded to or followed up on the findings raised by internal audit.	
11.7 C	Where there is no internal audit function, explain the reasons for this and how the audit committee has determined that this remains appropriate.	
12.	**External audit: audit tendering and rotation**	
12.1 C	Disclose the length of tenure of the external auditor and when a tender was last conducted.	
12.2 G R	Include the current external audit partner's name and for how long the partner has held the role. If there is an upcoming partner rotation, consider including the name of the new external audit partner, if known.	
12.3 R	Explain how the audit committee will meet external audit tendering and rotation requirements and any impact of the relevant transitional arrangements.	
12.4 G	Disclose advance notice of any plans for retendering the external audit. *Note: This is also a requirement of the 2016 Code.*	

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13.	**External audit: fees and non-audit services**	
13.1 G	Explain the committee's policy for approval of non-audit services (approval criteria are recommended). Changes to the policy in the year should be described in the audit committee report – this would be expected following the introduction of new standards arising from EU audit reform. *Note : The 2016 Guidance on Audit Committees does not contemplate a website cross-reference for this information.*	
13.2 G	Disclose the audit fees for the statutory audit of the company's consolidated financial statements.	
13.3 G	Disclose the fees 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. *Note: The Financial Reporting Lab also recommends disclosing a ratio of audit to non-audit fees over time as useful to investors, however few companies currently do this.*	
13.4 G	For each significant audit related or non-audit engagement, or category of engagements, disclose an explanation of the services provided and why the audit committee concluded that it was in the interest of the company to purchase them from the external auditor. *Note: The audit committee should decide what makes an engagement "significant" in order to maintain consistency of disclosure and so that the rationale can be explained if any queries arise.*	
13.5 G	Explain how auditor objectivity and independence has been safeguarded where the external auditor provides non-audit services and a comment about how the audit committee has satisfied itself regarding the independence of the external auditor.	
14.	**Effectiveness of the external audit process**	
14.1 C G	A clear explanation of the process undertaken to evaluate the effectiveness of the audit process could include the overall approach that has been taken to audit quality, timings and actions arising. Consider referring to a framework, such as the FRC framework, if one has been used in the assessment. *The key messages to convey are how the audit committee is satisfied that an effective audit has been completed, that the scope of the audit is appropriate and that significant judgements have been challenged robustly.*	
14.2 R	Explain what has been assessed, for example the performance of the external auditor alone or also management's preparedness for audit.	

Key:

C	2014 UK Corporate Governance Code – the Code companies will report against until periods commencing on or after 17 June 2016
G	2016 Guidance on Audit Committees – the current version of the FRC's Guidance, released to support the 2016 UK Corporate Governance Code
L	FRC Financial Reporting Lab report
F	FRC area of focus
R	Deloitte recommendation for good practice
DTR	Disclosure and Transparency Rules

	Content requirement/recommendation	Your comments and notes
14.3 R	Describe involvement of those outside the audit committee, for example management or internal audit, or a finance team survey.	
14.4 R	Refer to external evidence where used, for example the audit firm's transparency report, an audit inspection review on the audit firm or on the audit of the company itself.	
14.5 R	Explain the conclusions reached as a result of each key step taken and any actions undertaken by the audit committee, management or the auditor.	
14.6 R	Include a clear indication of how the assessment of effectiveness described above has impacted the audit committee's approach to the appointment or reappointment of the external auditor plus the final decision on this.	
15.	**Interaction with regulators**	
15.1 G	Describe the nature and extent of interaction (if any) with the FRC's Corporate Reporting Review Team. Some companies indicate when there has been no such interaction, although this is not a requirement.	
15.2 G	Where the company's audit has been reviewed by the FRC's Audit Quality review team, ensure you have discussed the findings with the auditors and considered their significance, and if significant, made disclosures about the findings and the action that you and the auditors plan to take (without disclosing the score awarded).	
16.	**Additional considerations for FTSE 350 companies**	
16.1 CMA Order	Include a statement of compliance with the requirements of the Competition & Markets Authority's Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014. *Provisions include audit tendering at least every 10 years and audit committee responsibilities regarding audit tendering, recommendations on auditor appointment, negotiation and agreement of the audit fee and approval of non-audit services.*	
16.2 CMA Order	Where there has been no competitive tender process in relation to five consecutive financial years, the year in which the company proposes to complete a tender and the reasons why that year is in the best interests of the company's shareholders. *This information must be repeated each year until a tender has been completed. If the audit committee decides that a different year would be more appropriate, it must provide reasons for the decision in the first audit committee report published after the decision is made.*	

Key:

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Designed and produced by The Creative Studio at Deloitte, London. J10281