

A view on the current and future role of audit committees – impact for Germany, Switzerland and Austria

European Corporate Governance
2019 analysis



In cooperation with:



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EXECUTIVE SUMMARY

With the advance of digital technologies changing the nature of business in many industries and enhanced public concern over the behavior and environmental impact of the private sector, companies are facing both new risks, and greater scrutiny over their operations. Because of these changing risk profiles, in parts of Europe today, audit committees (ACs) are undergoing a period of transition. They are transforming from backward-looking committees focused on a narrow financial remit, to more forward-looking bodies tasked with evaluating a wider set of risks. This transition, along with the different board structures among geographies, has led to a variety of outlooks and perspectives among European ACs, though many common threads remain.

This study is designed to illuminate these different outlooks and perspectives, showing where they exist both geographically and in terms of content. The study also illustrates where opportunities exist for best practices to be formed that can help ACs respond to the changing risk profile of firms. To accomplish this, the report is derived from information gained from over 20 discussions conducted by Oxford Analytica with current AC members in France, Germany, Italy, the Netherlands, Sweden and the UK, as well as discussions with academic experts in corporate governance and board systems, and in-depth desktop research into each of the countries studied. It assesses what similarities and differences exist in the approaches and perspectives of European ACs and identifies areas where best practices can emerge to help ACs stay fit for purpose as the nature of their work changes.

Structural differences and competing views on roles of the AC

With differing national board structures including one- and two-tier boards, and variations in size and rates of activity, ACs in Europe both look and feel different from each other.

These divides are most clear in the breadth of role taken by ACs, with some ACs already having accepted a broader set of responsibilities, and others remaining focused on their traditional activities. ACs within the Netherlands appear to have the largest remit in terms of competencies, as they are asked to evaluate risks over a long-term time horizon and in external parts of the firm's operating environment, making them more naturally concerned with non-financial risks. This is in contrast with ACs such as those in Switzerland and the UK, which have a narrower focus on company financials, related risks and internal controls, staying heavily focused on the traditional work of an AC and external auditor supervision.

This divide in outlook, between a narrow definition of the role and a more expansive one, sets the tone for how ACs view the evolution of their role, the skill sets required, and how to engage with less defined tasks.

Broad similarities toward traditional roles and external stakeholders

Despite these structural differences, there are established norms in how ACs engage with important internal and external stakeholders.

Relationship with management, internal and external audit

While some AC members, particularly in two-tier board structures such as Germany, view their role and that of the board toward management as mainly supervising the execution of company strategy and policies, other European ACs generally view their role as multi-faceted

and requiring different approaches depending on the circumstances and what is being discussed. Most ACs understand their role as being a collaborative or consultative partner with management on the setting of strategy and objectives, such as risk control frameworks and thresholds, and then a supervisory one when it comes to the execution of the resulting plans.

Similarly, while there is some difference over the amount of control ACs in Europe exert over the internal audit function in two-tier board systems, such as those in Germany and Italy, due to legal restrictions, there is general consensus around the best practice of direct control over the two audit functions and internal controls by the AC, with the committee representing the most important stakeholder for both audit functions. Therefore, when it comes to the traditional tasks of overseeing the internal audit and controls process as well as the external audit review of company accounts, the interviews conducted for this project show that ACs – regardless of system – take a relatively uniform approach to both those relationships and their responsibilities.

Limited engagement with external stakeholders

Broad consensus also exists among ACs in how to engage with key external groups, particularly investors and relevant regulators.

For the investor community, ACs remain silent despite being perhaps the most visible committee in any board structure. They (have to) leave engagement to management based on regulatory responsibilities, despite the external facing nature of their work and the evident stakeholder interest in financial accounts. Formal contact with regulators was also almost universally shunned at the company level, with ACs relying on informal discussions between AC Chairs and regulatory bodies to articulate their views. There is also some reliance on larger groups, such as the one that brings together the AC Chairs of the DAX 30 in Germany to provide formal commentary on new regulation and legislation.

Cracks emerge on less-defined tasks and risk outlook

While ACs across Europe find themselves approaching and supervising key internal and external stakeholders in a similar fashion, in areas where their tasks are less closely defined, such as fulfilling the EU Audit Directive and Regulation, significant differences emerge.

EU Audit Reform – demonstrating a difference in perspective

While no clear national divide appears to exist between the outlooks taken by ACs on the EU Audit Reform, the different means they use to address it – either an input- or an outcome-based approach – serves as a clear indicator of a difference in perspective among ACs in Europe. Those

concentrating on outcomes are monitoring the outcomes of the overall audit process to ensure the integrity of the financial reporting process, while those following an input-based process will hold extensive discussions with the external auditor prior to commencement of the audit.

Setting the agenda – from tactical issues to looking ahead

Discussions with ACs across Europe revealed two perspectives are used to frame the AC agenda: one that is tactical, focusing on current business issues or newly-enforced legislation, and another that is concerned with emerging trends and issues that could develop over a longer time horizon.

It is here where the breadth or narrowness of an AC's remit serve as the main differentiating factor, and not structural differences such as a one-tier or two-tier board structure. Thus, traits such as the responsibility of Dutch ACs to consider cyber risks and external stakeholders create a demand for Dutch ACs to be forward-looking and consider risks that are not yet present, while ACs in systems with a narrower set of responsibilities, such as the UK and Italy, are focused solidly on solving tactical issues related to changes in regulation, M&A activity, or other firm-specific tasks. Firms in France and Germany straddle this divide, oscillating between the two approaches.

Opportunities for improvement

Finding the effective balance between today's operational and reporting challenges and tomorrow's unseen risks is the greatest challenge facing European ACs today.

To accomplish this task, and stay fit for purpose, European ACs should:

- ▶ Establish a clear best practice for their involvement in overseeing CSR reporting and the creation of an audit (in contrast to a review) for those statements.
- ▶ Acknowledge the need to add skills relevant to the digital tools, processes and systems impacting internal business functions and the role of internal and external audit.
- ▶ Consider adjusting board committee tenure to help bring those new skills into the AC more quickly.
- ▶ Engage more openly and formally with regulators and policy makers to help minimize any negative impacts from the increasing pace of regulatory change.

By embracing the need to move into new areas of responsibility, European ACs can establish even greater trust in the financial reporting process, which is their traditional and core function.

Most importantly, they can also better prepare the firm for the future risks that will inevitably emerge.

Introduction

Just as business models are changing, so are the expectations that both society and government have for corporations. With the advancement of digital technologies and Industry 4.0, the tools of business are being transformed, forcing established firms to adopt new processes and develop new products to keep up with the pace of change. While the burden created by these impacts falls heaviest on company management, members of supervisory boards and non-executive members of Boards of Directors must also grapple with these changes and how they impact the current and future operating environment of the business.

Accordingly, corporate boards are being increasingly asked to monitor and provide guidance on issues beyond their traditional tasks, raising questions about established board structures, and in particular the work of audit committees. These committees may now be challenged with oversight requirements outside of their traditional role overseeing financial reporting and internal quality control and risk management systems. Thus, despite being an established part of effective governance structures, a variety of approaches and perspectives emerge in Europe on how to best use an AC.

Role of audit committees and their importance

As the corporate body responsible for the verification of company financials and oversight of the internal and external audit processes, ACs are an important recipient of material from management and external sources, and thus serve as a conduit for information between the firm, its external auditors and the board of directors or supervisory board. An AC that is proactive and competent can help guide the firm through regulatory changes and ensure trust in its financial reports, while ACs that are less active, or less competent, can inhibit the board from having sufficient insight into company accounts and reduce confidence in their validity.

Outside of the financial services industry, where separate risk committees have become an established best practice and are now required under EU regulation, ACs have also begun to take on a new portfolio.¹ They are increasingly being asked to monitor new issues such as data privacy and digitalization, exposing them to new (compliance) risks. This is also forcing them to think in a more forward-looking manner, moving ACs away from traditional audit, which is a back cast of financial information, and into horizon scanning around regulatory or business issues that could negatively impact a company going forward. This is creating ACs with diverging perspectives and personalities.

¹ European Banking Authority, Guidelines on internal governance under Directive 2013/36/EU, 26 September 2017.

Unseen impacts of culture and company structure on board systems

The scope and impact of these shifts are further heightened and varied by the different board systems present throughout Europe. With the presence of both one-tier and two-tier structures, the composition and responsibilities of ACs within Europe shift from country to country, with some having a narrower remit, and others being asked to more proactively handle and evaluate risks and events in the wider business environment.

These different structures and views on the role of ACs raise questions such as: What role should an AC play in overseeing areas of emerging risk? And, are there best practices that can be taken from the work of ACs in particular European structures that can be brought to other systems?

Given these changes it is important to understand how ACs in Europe today are functioning. This includes:

- ▶ their structure and scope of responsibilities;
- ▶ how they engage with management, the internal audit function, and the external auditor;
- ▶ what relationship they have with external stakeholders (if any);²
- ▶ how they stay current with changes in regulation and legislation; and
- ▶ what items are currently on their agenda.

This report will seek to answer those questions by identifying the extent to which ACs are prepared to embrace the ongoing changes to their role and offering suggestions for how ACs can develop best practices where gaps exist, so that they can stay fit for purpose during this period of change.

The information used within is derived from over 20 interviews conducted by Oxford Analytica during February and March 2019 with current AC members in France, Germany, Italy, the Netherlands, Sweden and the UK, discussions with academic experts in corporate governance and board systems, and in-depth desktop research into each of the countries studied. The report uses qualitative

interview information to get a sense of AC agendas in different countries. The report does not seek to simply describe formalities, such as gender, tenure and meeting schedules. While some of these data points are used, that is to help reflect more deeply on the capacity of ACs to react to the changes in company risk profile that are currently taking place.

Two in-depth interviews with AC members from Germany and the Netherlands are also included, giving additional insight into what AC members in those countries see as the important contemporary issues, how ACs should respond to them, and how they view their role changing over time. Chosen due to their different views on the scope of AC responsibilities, they help to illustrate both areas of convergence and difference between different European board systems.

² In some structures, such as in Germany, direct contact between the AC and external stakeholders is not allowed. In others, it is less prohibited, giving rise to the possibility for it to exist.

Why do we have audit committees?

ACs are now a near-universal feature of corporate boards. Yet their purpose, which is to provide assurance and clarity about the financial workings of a firm, and to offer a safeguard against mismanagement, has its roots in earlier financial crises and the collective action problems found in different board structures.

Origin of the Audit Committee – forged by scandal

A precursor to the modern AC, Italy's Collegio Sindacale, was first established in 1882. It serves as the first European example of an AC in a system that remains in use today, although the advent of the modern AC as we would recognize it stems from the US, where it emerged as a tool to increase public trust after a series of costly scandals.³

The concept of an AC was first endorsed by the US Securities and Exchange Commission (SEC) in 1940 following a fraudulent audit led by management at the US firm of McKesson & Robbins. By the 1970s, after further scandals, involving illicit payments by US firms that went unreported in their company accounts, the SEC prevailed upon the New York Stock Exchange to include the creation of an AC in its listing requirements.⁴ This standardization in the establishment of ACs in large American companies led to the spread of the AC as a form of corporate governance from the mid-1970s until the early 1990s, during which time they were adopted as best practice by firms in Europe. By 1995, all members of the FTSE 100 in the UK had established an AC.⁵

ACs were further strengthened following subsequent reporting scandals such as at ENRON, which spurred the creation of Sarbanes-Oxley in the US in 2002, as well as Parmalat and Ahold in Europe. Since 2003, the establishment of an AC has become a near universal component of national corporate governance codes and enshrined in EU regulation for public-interest entities.⁶

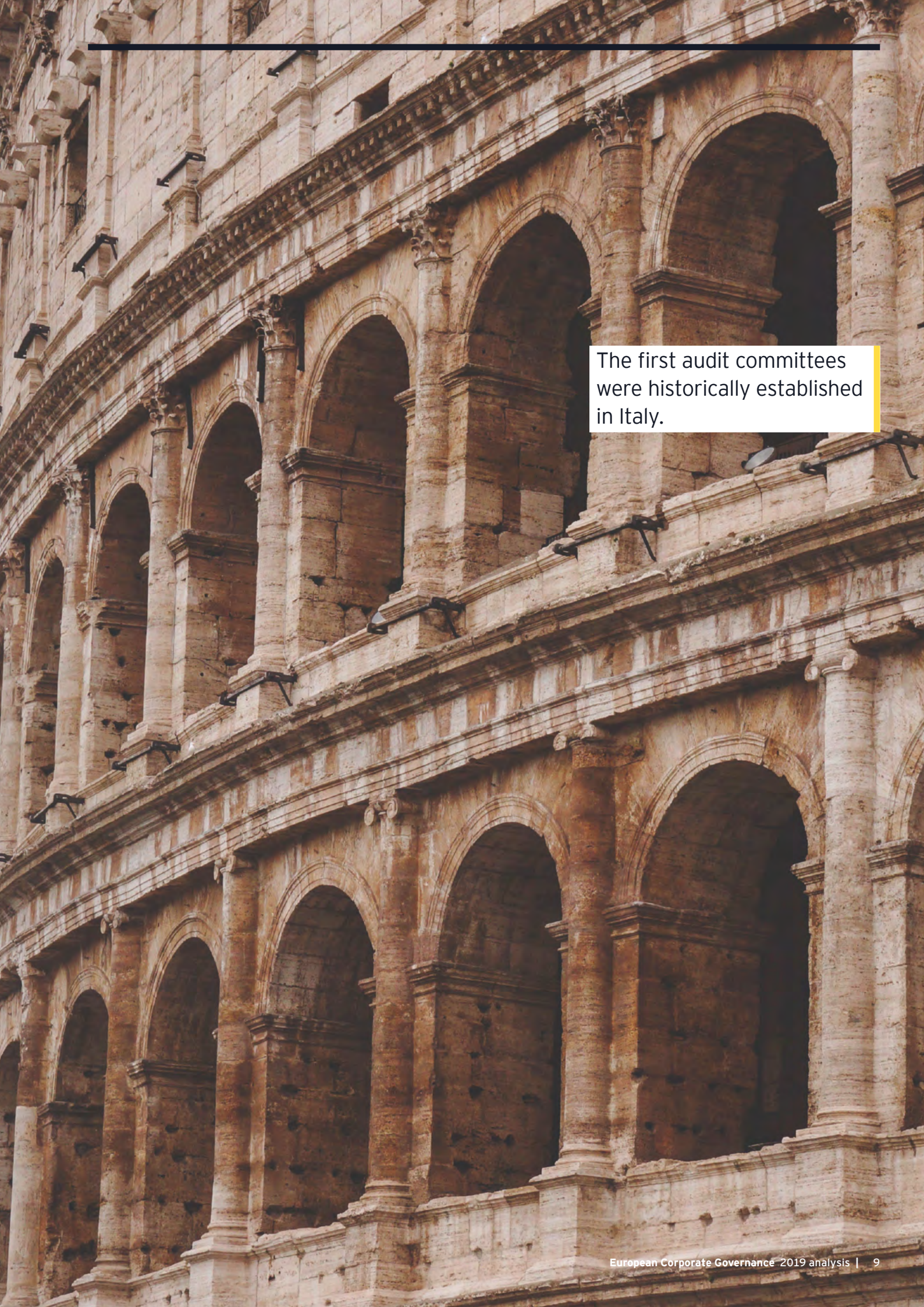
ACs have thus been shaped and solidified by periods of low investor or regulator confidence in business and have been systematically enhanced to assure investors and the wider public.

3 Consiglio Nazionale Dottori Commercialisti, Corporate Governance in Italy – the Board of Auditors, October 2003.

4 Wright, Mark; The Oxford Handbook of Corporate Governance, 28 March 2013.

5 Spira, Laura; Ceremonies of Governance: Perspectives on the Role of the Audit Committee, 2000.

6 Directive 2014/56/EU and the EU regulation of the European Parliament and of the Council of 16 April 2014; German Corporate Governance Code, as amended on 7 February 2017.



The first audit committees
were historically established
in Italy.

Differing structures and responsibilities: where audit committees first diverge

ACs have specific roles, responsibilities and perspectives under different national systems. Understanding the differences between structures and how they impact the role and activity of ACs is a key component of distinguishing AC culture, outlook and work across geographies.

Common traits and responsibilities

Some universalities exist for ACs across governance structures. In particular, boards and ACs are often subject to legal requirements defined in EU and national legislation or national governance codes, as well as sector or industry specific codes, which are mostly quasi-mandatory. Similarly, in all countries included in this study, ACs are required to have independent members, and to include at least one individual with a significant background in finance and accounting, often referred to as a financial expert.

Given their primary purpose, ACs also share a specific set of finance and accounting responsibilities that relate to the overseeing of financial reports, and the internal and external audit as well as internal control and risk management process per EU reform and as described thereafter in the text. While these responsibilities and how they work in practice do vary, as does the language used to describe them in national governance codes, the following can generally be considered the standard role of an AC, regardless of structure:

- ▶ oversight of internal controls and risk management processes;
- ▶ selection or recommendation of the external auditor and oversight of their independence;
- ▶ management of the external audit process; and





- ▶ monitoring of company accounts and approving financial reporting statements.

Beyond these core tasks, however, strong differences in board type, responsibility and size also exist which impact what tasks ACs engage in and why, as well as how they see their future needs.

To set the scene for the further analysis in this report, the following is a brief overview of the different dominant board systems in place within the countries covered in this report, together with the idiosyncrasies of their ACs.

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Corporate governance varies significantly throughout Europe, with each national system having slightly different roles and perspectives for ACs.

Key differences in governance model, scope, size and level of activity

ACs in Europe structurally diverge in three key areas: governance model, scope of responsibilities, and in their size and corresponding level of activity.

One- and two-tier boards: different models and perspectives

The first and most obvious area of difference is between that of one- and two-tier board structures.

One-tier boards – dispersed ownership and shareholder dominance

One-tier board structures developed in countries with a “market-based” finance model and a high degree of ownership dispersion. This created an outside system where shareholders are at a disadvantage compared with management, and thus need the board to be closer to the work of company executives.

One-tier boards are the dominant system in four countries included in this study: France, Sweden, Switzerland and the UK. It is worth mentioning that France allows a choice between the one-tier and the two-tier structure with the one-tier being predominant. Sweden follows the Nordic Model, which is a mixture of one- and two-tier system with the important feature, that the board is entirely or predominantly composed of non-executive directors.

Two-tier boards – concentrated ownership and a stakeholder perspective

Conversely, the two-tier board structure model has historically been driven by a “bank-based” finance model and high degrees of ownership concentration. This creates a system by which there are a few concentrated large interests with the need to manage those collectively. This has helped to form a stakeholder-driven model, particularly within systems with employee co-determination on the supervisory board. Within the two-tier system there is a clearer distinction between executive and non-executive directors on the respective boards.

This type of two-tier board structure is the dominant system in three countries studied: Austria, Germany and the Netherlands. It is worth mentioning that the



Most European ACs have delineated responsibilities that remain focused on traditional financial topics.

Netherlands allow the choice between one-tier and two-tier board structure. Although companies may generally adopt either structure, after exceeding certain size-related thresholds, companies are obliged to adopt a two-tier board. Overall, the two-tier boards predominate.

An exception to this is Italy, where the dominant board system is a unique horizontal structure whereby the second board, the Collegio Sindacale, sits alongside the board of directors, and has a narrow remit to see that company decisions are in line with legal expectations and oversee the external audit as well the internal processes that contribute to audit and accounting. Interestingly, Italy allows the choice of three different board structures: the “traditional” model with a board of directors and a board of statutory auditors (Collegio Sindacale), as well as a typical two-tier and a typical one-tier system.

From narrow to expansive – a growing divide in the scope of AC responsibilities

Beyond the structural divide that impacts how members of ACs and boards in general view their responsibilities toward management, there is also a growing separation among ACs in the scope of their work. This can vary due to regulatory cross-country differences from an expansive focus on new and emerging risks to a narrow focus on purely financial tasks. This division impacts not only the current work of ACs in Europe, but also how they see their role developing and how they prepare for any perceived changes.

Two generic categories of AC exist in terms of how the scope of their roles are viewed:

- ▶ Expansive view of role and responsibilities: France, the Netherlands and Sweden
- ▶ Traditional view of role and responsibilities: Austria, Germany, Italy, Switzerland and the UK

France, the Netherlands and Sweden – changing the scope of AC responsibilities

France, the Netherlands and Sweden provide the largest scope for ACs to undertake tasks outside of their traditional function. Within this group, Dutch ACs have the largest delineated remit, as they are directly responsible for exposure to cyber risks and digitalization, making them increasingly forward-looking.⁷ Dutch supervisory boards as a whole are also tasked with considering risks to long-term value creation, including impacts on other environments within which the firm operates, which helps to shape how Dutch ACs view their role.⁸ Similarly, Swedish ACs operate under a less-defined governance structure, and thus often find themselves taking on tasks apart from their traditional audit and financial reporting functions. Monitoring CSR reporting and emerging risks is quite common for Swedish ACs, which can also be found, as in the case of Volvo, to be monitoring company culture and ethics as a part of the non-financial disclosure process.⁹ Meanwhile in France, ACs are tasked with monitoring for ‘additional risks’, creating a means by which their role extends outside of audit and into a more general risk function, allowing them to take a broader view of risk issues, and play a role in other areas, such as changes in business profile.¹⁰

Austria, Germany, Italy, Switzerland and the UK – a more traditional focus

In comparison to the other group, ACs within Austria, Germany, Italy, Switzerland and the UK all have delineated responsibilities that can be considered relatively standard, and which roughly correspond with the common traits

7 Monitoring Commissie Corporate Governance Code, 2016 Dutch Corporate Governance Code, accessed 14 January 2019.

8 Monitoring Commissie Corporate Governance Code, 2016 Dutch Corporate Governance Code, accessed 14 January 2019; Interview with member of Dutch Audit Committee.

9 2017 Volvo Group Corporate Governance report; Spencer Stuart, 2017 Nordic Board Index, 2017; Swedish Corporate Governance Board, The Swedish Corporate Governance Code, 1 December 2016; OECD, Corporate Governance Factbook, 2017.

10 AMF, Study on chairmen's reports on internal control and risk management procedures for financial year 2012, 24 December, 2013.



Audit committees in the Netherlands are required to evaluate company impacts on external stakeholders and oversee cyber risks.

described above, focusing on tasks such as monitoring financial accounts, oversight of the external audit process and review of internal controls and risk management.¹¹ For Austria, Germany, Switzerland and the UK, the AC has not received any enhanced responsibilities asking it to consider specific non-financial or emerging risks, keeping it relatively confined to areas of financial oversight. For Italy, given the very specific and purely oversight role of the Collegio Sindacale, an ever narrower focus is proscribed, based primarily on compliance with standards and the adequacy of internal systems.¹²

Different scale of responsibilities leads to different outlooks on future role and needs

These distinctions between ACs in scope of role and varying skill sets are important, as they help explain not only current divides in AC agendas across Europe, but also significantly impact how AC members view their own responsibilities and how their role may and should develop. The divide between the systems is thus evident in how AC culture, outlook and work vary across geographies, and serves to indicate which ACs have a more forward-looking outlook and which are still driven by tactical financial concerns.

Larger the Audit Committee, fewer the meetings

There is also a clear divergence in the size and level of activity of European ACs, which serves as a proxy for their engagement and ability to handle increased tasks.¹³

Based upon an analysis of firms listed on the major national stock index of each country studied (e.g., DAX, MIB, etc.),¹⁴ the average size of ACs in Europe fluctuates between each system, ranging from a low of three in Italy to over six in Austria, with regulatory requirements set in national corporate governance codes influencing these figures. While Italy is structurally unique due to the extremely frequent meetings of the Collegio Sindacale and is thus not in the subsequent chart, a comparison of the different countries shows that, there is an inverse relation between size of the AC on one hand, and the frequency of meetings on the other, though Germany does have rather active ACs for their size.¹⁵ This difference extends beyond the divide of one- and two-tier board structures, or those with a narrower or broader remit, indicating that size rather than structure or scope is the biggest driver of activity. While additional factors such as regulatory changes and firm financials might lead to yearly swings, these do not represent structural factors.

11 The UK Corporate Governance Code, April 2016; Swiss code of best practice for corporate governance; Austrian Code of Corporate Governance, January 2018; German Corporate Governance Code, as amended on 7 February 2017.

12 Consiglio Nazionale dei Dottori Commercialisti, Corporate Governance in Italy – the Board of Auditors, October 2003; Consiglio Nazionale dei Dottori Commercialisti, Corporate Governance in Italy – the Collegio Sindacale, April 2009.

13 Firm size, industry and complexity were not controlled for during this analysis. Therefore, it cannot be excluded that AC size and meeting frequency may be less divergent if these factors were considered.

14 For more information and detail please see Appendix 1.

15 The data used to make this conclusion was taken from the annual reports of the firms listed on the largest national stock index for each country studied, which was then aggregated per country to create an average. For additional information on the data collected, please reference Appendix 1.

Figure 1
Larger the Audit Committee, fewer the meetings

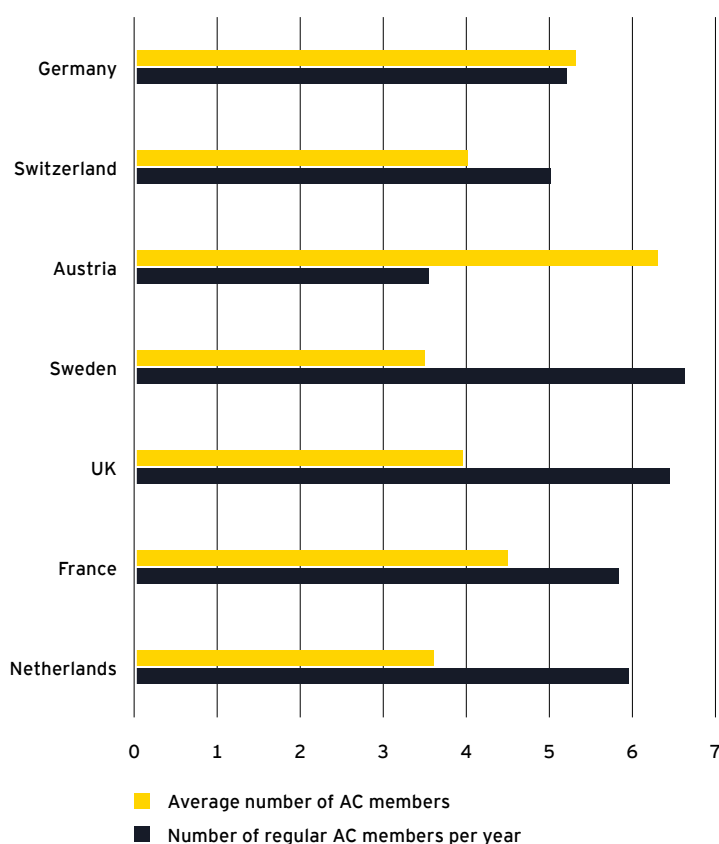
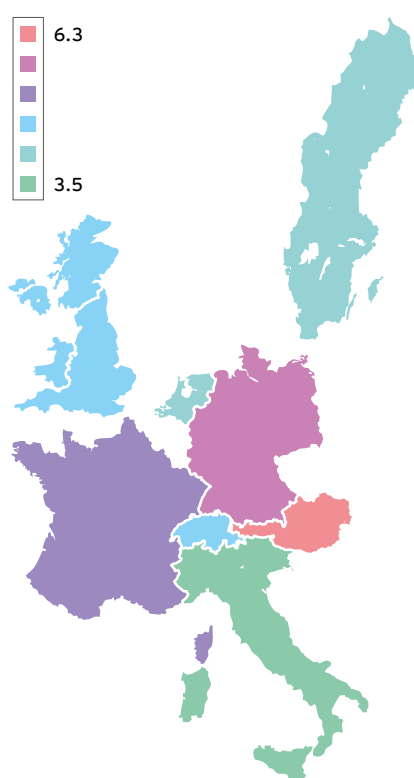


Figure 2
Average Audit Committee size



For additional information please see Appendix 1.

This is significant, as ACs that meet more often are more likely to dive into deeper issues or handle larger tasks. It also signifies areas where human capital is underutilized, and room for growth exists, as larger ACs such as in Austria should have the capacity to meet more frequently or make further use of their membership, and thus handle an enlarged portfolio. Similarly, it also demonstrates instances, such as in the UK, where the AC already meets frequently on a narrow set of financial topics, and where capacity for growth is limited.

It is thus clear that ACs within Europe face three structural divisions: that of board system, breadth of role, and size and activity of the AC. While the benefits and drawbacks of these differences will be discussed further,

it is already evident that while issues in capacity and activity impact the outlook taken by ACs and their attitudes toward non-traditional areas of AC responsibility, divisions in the breadth of roles undertaken by ACs is the area with the greatest impact on how ACs see their role and its future needs.

Outlook on key relationships with management and audit

A photograph showing the silhouettes of several people inside a cave, climbing over rocks and reaching towards a bright light at the cave's exit. The scene is dimly lit, with the primary light source being the opening of the cave, creating a strong backlight effect on the figures.

With these structural differences in mind, we can now evaluate how boards and ACs vary in terms of culture and outlook as these relate to their role and relationships with management and with the different audit functions.

Not surprisingly, given the high degree of regulation of ACs, while there are differences in the relationships between ACs and some important actors, for the most part there is broad alignment on how ACs should engage with management and with the internal and external audit functions.

Engagement with management

One- and two-tier boards have different degrees of closeness in relation to company management, and this in turn creates the possibility for varying perspectives on the role of the board toward management. However, whether an AC is operating in a two-tier or one-tier structure, the understanding of its relationship to management is strikingly similar.

Consulting on strategy, supervising execution – perspective of the board

While some AC members, particularly in two-tier board structures such as Germany, consider their role to be mainly supervising the execution of company strategy and policies, there is a general consensus among AC members that their role, both within the AC and in the board at large, takes different forms depending on the circumstances and the issue being discussed.

AC members in both one- and two-tier board structures indicated that within their wider role as board members, they are responsible for providing guidance and for offering a questioning outlook to company management when issues are brought up for discussion, and for supervising management in the successful delivery of company strategy and objectives. The common perception of AC members on how they engage with management, both as an AC member and in their capacity as a board member, appears to be consultative in the setting of strategic issues, but then supervisory in overseeing the execution of those decisions once they

have been made by management. Within their role on the AC, AC members expressed that they had a consultative role on topics such as the setting of key risk areas, controls for those areas and defining the firm's risk appetite framework. This is in comparison to their work on the wider board, which consults with management on the company's overall strategy before giving its approval.

This perspective of having both a consultative and supervisory role is shared across one- and two-tier board systems, with interviews with AC members from the UK, the Netherlands, Germany, France and Sweden all indicating this approach to their board and AC responsibilities. Italy, with its narrow legal requirements for the Collegio Sindacale, was the only country where this perspective was not mentioned by those interviewed.

Although some boards, particularly in two-tier structures, appear to take mainly a supervisory role, both one- and two-tier boards are becoming increasingly involved in forward-looking discussions with management at the board level. This is encouraging and shows an increasing degree of active engagement from corporate boards, which is likely to be further reflected in the attitudes, perspectives and activities of ACs going forward as they are forced to adapt to handling different risks, such as data privacy and cyber security.

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Corporate boards across Europe view their role as a combination of providing guidance and consultation to management and monitoring management's execution of strategy.

Internal audit and the external auditor – differing perspectives

While AC members across board systems share a broad consensus on how they engage with company management and view their corporate governance role, the same cannot be said for how ACs oversee and interact with the internal and external auditor, with different approaches existing across governance systems.

Internal audit – a balance between management and board oversight

In the case of the relationship between ACs and the internal audit function, interviews suggest that there is on occasion a difference in the official reporting relationship between internal audit and the AC in one-tier and two-tier boards.

In one-tier systems, as in the UK, France and Sweden, the internal audit function reports directly to the AC or its chair, with a dotted line to company management such as the CFO. This structure cements the independence of the internal audit team, as its primary responsibilities fall to the board and not to company executives. In a two-tier board structure however, such as in the Netherlands and Germany, this system is sometimes reversed, whereby the internal auditor technically reports to management, either in the form of the executive board or a member of senior management such as the CEO or CFO, with the AC or its chairperson as their secondary reporting relationship.

While in practice – according to AC members who have worked in both systems – the behavior of the internal auditor and their role is relatively unchanged between the two, there is nonetheless a difference in the driver of the relationship. Internal audit teams in different companies in two-tier board structures show varying degrees of separation from management in their interactions with the AC, with some reporting to the AC with management present, and others not. AC members from two-tier board structures such as in the Netherlands thus expressed dissatisfaction with their more limited influence over internal audit, and a desire for this relationship to change going forward.

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Internal audit is not fully independent in some two-tier board structures.

Limited difference between systems in key relationships

Although any negative impacts from this difference in reporting relationship are unclear, a desire by some ACs in two-tier board structures for a more direct reporting relationship with the AC is noted and represents an area where some ACs wish to assert additional oversight.

Clear control over the external audit process

While the relationship between the AC and internal audit can vary between one- and two-tier board structures, control over the external audit process is somewhat clearer and more uniform. AC members across systems and geographies, including those in the UK, Germany, the Netherlands, Sweden, France and Italy all described a more direct relationship between the AC and the external auditor. These ACs are not only in charge of the selection process but are responsible for the work of the external auditor and are their key reporting relationship and stakeholder. This separates the external audit from management and the internal audit process and is designed to ensure that the external audit provides the AC with a thorough and unbiased view of company accounts.

Laggards do exist: some firms are failing to uphold best practice

Interviews with AC members from both the Netherlands and Germany indicated that in some firms the external audit relationship is de-facto in the hands of the management board instead of the AC.

This represents a downside among some ACs to follow best practice, as while the external audit is meant to be completely independent from company management, the forfeiture of direct oversight of the external auditor by an AC fundamentally limits the effectiveness of undertaking an external audit. There thus exists the need for some ACs to exert their traditional role more strongly and focus on fulfilling their stated responsibilities.

Overall, while there is some disparity between board systems in how ACs interact with key stakeholders, particularly in the reporting relationship between the AC and the internal audit function between one- and two-tier boards, for the most part, across systems and geographies there is broad consistency on what constitutes best practice in the role of the AC. These best practices, whereby the AC adopts a balance between a consultative and supervisory role toward management, exerts control over the external audit process and ensures the independence of the internal auditor, are all important: They allow ACs to be in the best position to accomplish both their traditional tasks and the new topics emerging onto the AC agenda.





Where paths diverge – areas of limited guidance

Whereas AC role and responsibilities toward management, internal audit and the external auditor are all well understood and in most cases uniform across countries, there are tasks undertaken by ACs that are less clearly-defined due to high topicality and are more open to interpretation or a divergence of opinion. These responsibilities, such as implementing, measuring external audit quality, and handling CSR reporting, represent areas where ACs are still searching for best practice, and are generally unhappy with the current tools and processes at their disposal.

Applying the EU Audit Reform

For all public companies in Europe, regardless of structure, one constant is compliance with the 2016 EU Audit Regulation and the respective national laws that were enacted to ensure compliance.

While varying somewhat due to differences in how it was transcribed into national legislation in different Member States, the EU Audit Regulation requests that an AC shall, *inter alia*:

- ▶ inform “how the statutory audit contributed to the integrity of financial reporting”; and
- ▶ “monitor the financial reporting process and submit recommendations or proposals to ensure its integrity.”

A vague request and varied replies

This request of ACs by the EU is somewhat vague and open to interpretation, and as such has led to a variety of perspectives on how to best meet these criteria.

Primarily, ACs believe that by going through the formal reporting process, by flagging issues raised by the external auditor, and by holding management accountable for an action plan to fix those issues, they will satisfy the need to monitor the financial reporting process. This belief that oversight of the firm’s public-facing accounts is sufficient was mentioned by ACs in France, the UK, and Germany, and represents an outcome-focused approach.

In other words, monitoring of the end product and ensuring its quality is the way in which the statutory audit contributes to the integrity of financial reporting.

Other ACs took a different perspective on meeting these requirements, focusing instead on the inputs into the process, particularly the audit plan and the key metrics they wish the external auditor to examine. As mentioned by ACs in the Netherlands and Italy, this input-driven approach to compliance centers around extensive discussions with the external auditor prior to its commencement of the audit, and a clear delineation of the areas and issues the AC wishes the auditor to pay particular attention to. These inputs are then considered by the AC when they examine the financial reports and the external audit, giving the AC the opportunity to monitor whether its concerns were looked after by the auditor.

While there is no clear national divide between the outlooks taken by ACs, compliance with this aspect of regulation is an area where ACs show some uncertainty over how to proceed, and thus additional guidance from the EU or national regulators could be useful. ACs are confident that they do comply with the regulation and that their means of ensuring the integrity of the financial reporting process is strong, yet no best practice seems to exist on how to standardize this process across firms and systems. This is an area where the EU or regulatory bodies could more clearly define a best practice for ACs to follow.

“

When following the EU Audit Reform, firms in Europe oscillate between input- and outcome-focused approaches.

Measuring the external audit quality

Another area that is not fully defined is measuring the audit quality as done by the external auditor.

Although ACs in every structure rely heavily on the work of the external auditor, ACs across Europe tend to depend on relatively informal and unquantifiable means to assess the quality of the external audit, as the proxies for audit quality – such as the number of restatements and the presence of significant deficiencies – are not seen as adequate. Beyond the questioning process undertaken by every AC during its review of the external audit, these informal and ‘soft’ metrics broadly fall into three categories: the skills of the auditor, the perceptions of the audit by management, and regulatory reviews of audit quality.

Auditor skills and knowledge

The first of these, and one mentioned by the majority of ACs during the interviews, is the skills and experience of the audit team. ACs seem to place great weight on the experience and industry knowledge of the partner leading the external audit, with some having used a lack of experience within the team conducting the external audit as a reason for seeking a change in auditor. ACs in Germany and the Netherlands also weight the tools and resources at the disposal of external auditor, both in terms of personnel and in the availability of digital audit capabilities. While the availability of qualified personnel and access to a sufficient skill set seems to be of primary importance to ACs, and is certainly a relevant component of audit quality, a narrow focus on these traits means that judging ‘audit quality’ – although widespread – is based solely on the belief and trust in the skills of the lead auditor and their team, and is thus a judgment based on the quality of what should be produced, and not necessarily on what is. This represents a noticeable gap in how the majority of European ACs measure the quality of the external audit process.

Perceptions of management and internal controls

The mechanism next most commonly used by ACs when determining audit quality is an internal survey, and discussions with both the internal auditor and senior management to gauge their perceptions of the external audit. This dialogue with management and the internal

controls team is designed to give the AC a wider understanding of how the company viewed the audit process, and whether or not the external audit had a sufficiently high skepticism of company management and the firm's own financial reporting. While ACs – in rare circumstances based on the interviews – expect some amount of disagreement between management and the external auditor, judging the desirable level remains an inherently subjective process.

Independent audit quality assessments

Outside of these internal and qualitative assessments of audit quality, ACs make use of the reports produced by the country's corporate governance regulator or standards institution. In the case of the UK, where interviews suggest these reports are most heavily used within the countries studied, ACs monitor the findings of the Financial Reporting Council to evaluate the overall performance of their external auditor and determine if issues raised in that report need to be asked to their specific audit team. This process, which received support from some AC members in France and the Netherlands, is the only objective tool commonly used to judge audit quality, but was viewed skeptically by many, as the findings of the oversight authorities are often not relevant to the external audit process at many firms.

Given the subjective nature of some of these tools and limited applicability of audit quality assessments to many firms' external audit process, measuring audit quality remains an area of judgment for AC members across Europe and an area where ACs continue to spend a significant amount of time and attention.



Involvement in CSR reporting

While applying the EU Audit Reform and measuring audit quality are either formal or implicit tasks for an AC, its specific role in evaluating CSR statements as compared to the entire is somewhat less clear in practice.

The 2014 EU Directive¹⁶ on non-financial reporting requires large companies to disclose information on how they operate and manage social and environmental risks. This non-financial disclosure forms the basis for what can be considered a CSR statement, and means that firms within all the countries studied are already compiling and producing this type of information.

However, while CSR is an area where the AC has at least some degree of responsibility, if only because of its inclusion within the annual reporting documents, there nonetheless appears to be little consensus across systems and within countries on how CSR reporting should be dealt with, including the exact role the AC should take in regard to preparing or auditing the report.

Done through the external auditor or the annual reporting process

Within some systems, such as in Sweden, the external auditor is expected to review the CSR statement and comment on its accuracy. This standard is similar in Italy, where it has recently become enshrined in national legislation, as well as in Germany, where some larger firms employ specialist third party groups to review their CSR reports, as well as the external auditor to provide limited or reasonable assurance on the non-financial declaration. This third-party process gives the external group the task of conducting the audit, limiting the involvement of the AC to that of a reviewer.

In other jurisdictions, including in the Netherlands, the CSR statement is often included within the annual reporting process, and is thus reviewed in its entirety by the AC, forcing it to share in the burden of the accuracy of the audit. While a relatively minor difference, these

¹⁶ EU Directive 2014/95/EU on non-financial reporting

two approaches signify different levels of responsibility, with neither being hailed as particularly robust approaches by current AC members.

Review of CSR reporting – the common standard across Europe

While no common best practice on how CSR statements should be reviewed by ACs has formed, the one trend that has emerged is that CSR reports, when audited, are almost always done to limited assurance expressing a review opinion. That standard, however, does not fully confirm the accuracy of CSR statements, making them somewhat less impactful.

There is thus significant desire by European ACs to have a stronger role in CSR oversight and a clear process for auditing that statement to be developed. As such, the role of ACs in CSR reporting is only likely to grow in the short to medium term, which will potentially help spur on the creation of guidelines of CSR reporting supporting a reasonable assurance and providing an audit conclusion.

Need for additional guidance and standardization

In all three of these areas, applying the EU Audit Reform, determining external audit quality and oversight of CSR reporting, ACs are divided in their approach and understanding of what is important. This divide leads to a lack of uniformity, and means the work done by ACs across geographies or systems is not easily comparable in these different areas of responsibility. Given the clear desire by ACs for a strong role in overseeing CSR reporting, and the time they dedicate to issues such as determining audit quality, there is an overwhelming need for corporations to develop best practices so that ACs can better accomplish these core, and emerging, areas of responsibility.



Audit committees are becoming increasingly active in reviewing CSR statements, yet no best practice exists for how to audit them.

INTERVIEW

INTERVIEW

Prof. Dr. Sven Hayn

GSA Assurance Managing Partner
Strategy, EY



Given your work across geographies in Europe, do you see any differences emerging between ACs across Europe in how they view their responsibilities? If so, what are they, and is the pace of change between them accelerating?

If you look at different ACs in different EU Member States, the overall themes and challenges all AC members face are quite similar. It is about the EU audit reform, digitalization, new technologies, cybersecurity, and measuring audit quality. Not surprisingly, all of these themes have been explored within our report. Overall, the AC responsibilities and therefore the topical landscape widened in the past years. While the role used to be centered on traditional accounting tasks and internal controls on financial reporting, it has grown to new areas of responsibility such as CSR reporting – even though the CSR responsibilities are with the entire supervisory board.

So while AC responsibilities are widening, the traditional cross-country differences between them are narrowing in a global economy. As a result, there is no key difference I can see between the challenges, themes and responsibilities on an AC within Europe.

In your work with ACs, what aspects of the EU Audit Reform have been the most difficult for them to implement?

There are two specific dimensions that make the EU Audit Reform very complex for both, the external auditors, and ACs.

The first is applicable to every public interest entity (PIE). While the EU Audit Regulation is directed at companies, it also included some 75 plus Member State options which have now been put into national law through legislation. Based on this foundation within the Regulation we now face a patchwork of requirements across the EU Member States. So while there is the same basis criteria and ground rules, the national adoption of what is within the regulation is very different. To illustrate: non-audit services (NAS) need to be checked for compliance based on the respective national law of the EU Member State where the services are rendered by the auditor. This means that a NAS allowed in one Member State cannot be rendered to a subsidiary in another due to the very specific transportation of the Regulation's Member State option into national law. Providing tax services is one of the examples to explain the EU patchwork. Therefore, overseeing all of these differences is a challenge for both audit committees and external auditor.

The second, which is client specific, is related to how many PIEs a group encompasses. To clarify, a PIE is a company that is listed on the stock market, but also credit institutions and insurance undertakings qualify as PIEs. Most of the international groups headquartered in the EU are so-called "multi-PIEs." That means, the PIE status is not limited to the parent company and depending on the industry and the company structure, the additional number of PIEs can range from a few to the high double-digits. That makes it quite complex, as each PIE needs to apply the national guidance of the EU Regulation specific to their own operations.

As an external auditor, what practices do you think ACs should employ to help measure external audit quality?

That is a very good question and a tough one. There are different bodies and institutions working on Audit Quality Indicators (AQIs), but there is not a definitive or a complete list. Standard criteria that can be looked at and adhered to is the composition of the audit team, that means the education and the profession of the audit team members along with their seniority, global reach and availability. Other indicators that are considered include their expertise in IFRS, US GAAP and auditing standards. Clearly today the audit engagement team needs to embed other skills in delivering a digitized audit and having capabilities in audit analytics, as well as sector specific expertise, so that the audit lead partner can be a true business partner for the AC.

Two things we at EY have done successfully to help our clients with this is the scheduling of a client service team meeting and putting together our own Assessment of Service Quality (ASQ).

The first one of these, the client service team meeting, is a one or two day meeting between the senior partners of the client service team, the company management,

and members of the AC to discuss current developments and expectations. This has helped us get a first-hand account from the larger divisions and regions within the company and that has been very successful in giving us a good base to assess the quality of the respective auditors.


The second way we have helped our clients with this is through the creation of an internal EY tool we call ASQ. On an annual basis, we undertake a web-based survey or interviews to solicit with management feedback from the client. We then combine the two into a report with action steps and feedback to the AC and then review the issues within the report 12 months later. Which in turn gives a clear indication of audit quality of the entire team.

Given all the change happening within the audit, are there any trends or issues related to the traditional aspects of the role that you think also require attention?

One trend that we are focusing on as a firm is reducing complexity within the accounting standards. We recently went through a number of years with enormous changes to International Financial Reporting Standards, which has placed a lot of changes on companies, and created a trend whereby every single new accounting standard consistently asks for more disclosures. As a result, we have supported a number of clients to review their processes, enhance disclosure effectiveness and thereby increase the relevance and understandability of their financial reporting. As it is important to make sure the traditional balance sheet and income statement – to name just two of the primary financial statements – remain understandable.

From my perspective, we need to avoid a situation where the historical financial statements become a pure compliance exercise, and people simply ask if they received an auditor's report or not. There is a lot of rationale behind and value in the historical financial statements, and we should not underestimate that they are The backbone of the functioning of capital markets. We therefore need to make sure that we stay current and modern in how we present financial information.

Against this background, the focus is shifting from financial reporting to corporate reporting. Themes and topics including CSR reporting and long-term value are on today's reporting agenda. Not surprisingly, the composition and skill set of ACs are beginning to reflect these developments including sustainable finance, new business models and digitalization.



Visible output but an invisible actor – external engagement

As perhaps the most visible board committee due to the public nature of their work, ACs across Europe attract the interest of external actors, including investors and regulators.

Yet despite this outsized importance, there is surprisingly little formal engagement done by ACs, acting as a committee, or by members acting individually, with external stakeholders, with strong regulatory limits put in place in some jurisdictions

to limit contact. Informal contact is thus the only enduring form of engagement. This, therefore, represents a risk that ACs will not meet the expectations of either investors, regulators or policy makers and will have little say on future regulation and policy.

“

Audit Committee members have no regular contact with investors and equity owners, and do not believe that those actors wish to be in contact.

Contact with investors – often prohibited, and minimal when allowed

As a body whose work is important in the evaluation of companies by investors, it could be expected that ACs, either as a group or AC members as individuals, would have some contact with institutional investors or large shareholders, particularly in countries where such contact is permitted by law, such as the UK.

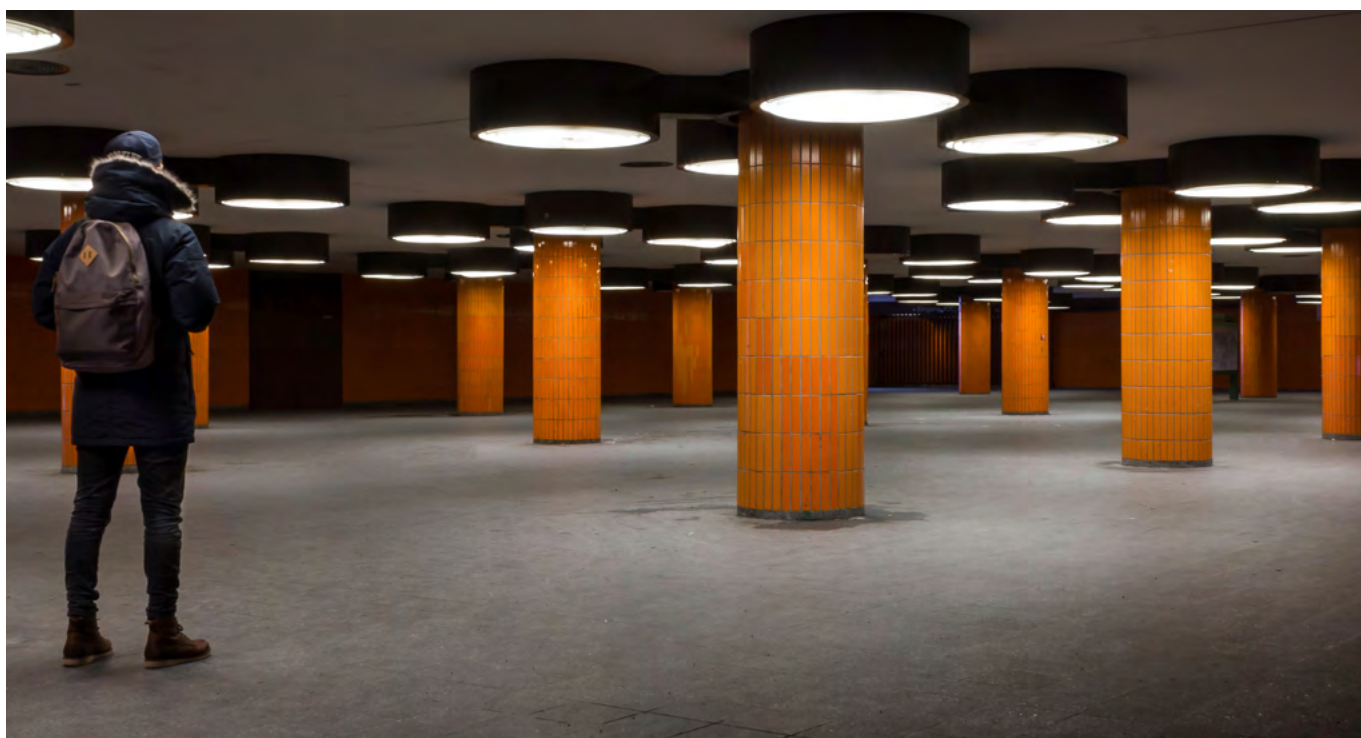
But discussions with AC members across Europe reveal that this is not the case, with ACs experiencing the opposite situation, remaining completely separate from investors and their concerns. While such a situation was expected in countries such as Germany, where the lack of contact between ACs and investors is in accordance with regulatory requirements, it was also the case in one-tier board structures that are more open to contact between investors and members of the board.

In the UK, whose structure is perhaps the most favorable to investor contact, the lack of contact appears to also be standard, with the only example given by an interviewee to

the contrary being the presence of the AC Chair at the annual general meeting (AGM) – though even in this instance, the contact with investors was minimal.¹⁷ This finding indicates that despite the importance of the work done by ACs, investors have little interest in speaking within them directly.

What role should Audit Committee members have with equity owners?

The lack of contact between AC members and investors in systems where there are no legal constraints is somewhat surprising and raises the question of whether the two groups should have any relationship, or whether the status quo should continue. With the majority of AC members in most countries, and all in the case of Switzerland, required by codes of corporate governance to be independent from both management and investors, there seems to be little demand from AC members for increased investor contact, nor belief from them that investors are interested in speaking with them.



¹⁷ Similarly, the entire board would attend the AGM as in other countries.

Regulators and policy makers – informal dialogue and unclear results

Outside of investors, the other external parties that are perhaps most relevant to the AC are the regulators and policy makers, who oversee tax, compliance, data security, and other issues.

Somewhat surprisingly, discussions with AC members revealed that ACs appear unwilling or unable to formally communicate with regulators and policy makers. Indeed, in systems such as Italy, where the Collegio Sindacale and the control and risk committee share the responsibility for the firm's audit, there is no relationship between those responsible for overseeing the audit process and the country's regulators. As noted by one AC Chair, even when requested for comments from groups such as national accounting standards agencies, ACs can be hesitant to reply. In some cases, this is because they regard regulation as being beyond their ability to influence, driving their decision not to intervene and communicate with stakeholders.

Instead, when communication with regulators and policy makers does take place it is almost always only at the personal and informal level, often between AC Chairs and members of the regulatory body. This type of dialogue, conducted at seminars or meetings hosted by the regulators themselves or third parties such as audit firms, is done sporadically, and almost always in the form of personal commentary or an informal discussion. It does not represent official correspondence or the views of any organization.

There are exceptions to this, with examples provided of groups of AC Chairs, such as in Germany for the DAX 30 companies, expressing their formal opinion to regulators immediately following or preceding changes in regulation relevant to the work of ACs. These formal communications to regulators are infrequent, however, and represent only collective views. Individual ACs do not appear to have a process in place whereby they, acting alone, can formally communicate with regulators.

Thus, while many AC members and Chairs across Europe expressed satisfaction with the informal dialogue they have with regulators, the lack of a regular process by which ACs can communicate with them and policy makers is potentially an obstacle to effective stakeholder communication.

This is particularly relevant as the degree of regulation that impacts the work of ACs will increase throughout Europe in both the short and medium term. Indeed, the pace of regulatory change is already an issue for ACs in many jurisdictions. The lack of a formal structure by which ACs communicate with regulators and policy makers is therefore an issue that ACs should seek to rectify in order to ensure a meaningful voice in future regulatory decisions.

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Groups of AC chairs, such as the one that exists for the DAX 30 in Germany, are the most common mechanisms that audit committees use to have a formal dialogue with regulators.

Outlook of Audit Committees – how to stay current, and structural restraints

A significant challenge facing AC members across Europe is staying informed of the key regulatory changes and emerging risk issues that could impact not only the financial reporting process but the security and stability of businesses.

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Audit Committee members often rely on the events and materials produced by external audit firms to help them stay current.

Staying current – leveraging the expertise of others

To keep up to date with regulatory changes, ACs rely on the expertise and knowledge of outside groups.

Role of the external auditor and audit firms

Events and publications on regulatory changes or emerging trends in audit and compliance by external audit firms, such as EY and other members of the large firms, are the most commonly used means of AC members staying current.

These events, which seem to be attended on at least an annual – if not quarterly – basis by many AC members, provide access to guidance on updated regulation, and also serve as a platform for networking with AC members from other firms and industries. For many AC members, particularly those who are not Chairs, these external events hosted by audit firms, as well as those occasionally hosted by regulatory agencies, are the main source of external information and networking on audit and compliance issues.

Similarly, the materials shared by the external auditor on upcoming regulatory changes or new trends within internal controls and compliance are the main source of literature for ACs on new developments. Internally-produced documentation on regulatory changes and impacts is often less frequently produced, making it a more secondary source of information for many ACs.

Continued access to these events and briefings is therefore highly important for AC members going forward, particularly as the role of an AC further develops.

Networking as a means of sharing best practice

Some Chairs of ACs have access to groups that regularly meet and serve as another mechanism for networking and staying current with audit and compliance trends, including across borders and systems. Groups such as Tapestry Network and EY's European Audit Committee Leadership Network serve this purpose and act as a vital conduit of information and sharing of best practice. Maintaining access to these groups is thus similarly important for AC Chairs.

Audit Committee demographics and structure do have an impact

Although there are no geographic or structural divides as to how AC members keep up to date with current regulations and emerging risks, the demographic and skills profiles of ACs in different geographies do seem to play a role in how effectively ACs are able to respond to change and take on new tasks.

Smaller audit committees – fewer resources

As boards of directors and supervisory boards have shrunk over the past decade in order to become more nimble, they have done so at the cost of board resources.¹⁸ Outside of AC members in the UK where the growing role of risk committees has stunted AC growth, AC members from across Europe mentioned how their increasing responsibilities represent in part a conflict with the decreasing size of boards of directors. The trend to decrease board size (within the constraints of mandatory board sizes by law as foreseen in Germany) naturally somewhat restricts the number of committees a board can create and still be effective, as well as the scope of work that committees can handle, as individual board members can become overstretched.



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Audit committees have increasingly scarce capacity to handle additional agenda items.

¹⁸ OECD, Corporate Governance Factbook, 2017.

Given that a further increase in AC responsibilities is likely to occur as risks become more pronounced and regulation more stringent, firms with larger ACs might, somewhat paradoxically, be better equipped to handle that shift. Provided AC members are sufficiently skilled, there will be more capacity on the AC for additional tasks outside of traditional financial oversight. Larger ACs, such as those in Austria and Germany and other two-tier board structures, may therefore be better positioned to handle this coming increase in AC responsibility than those elsewhere, which draw upon less human capital.

Takes time to add new skills

The increasing importance of emerging risks, such as exposure to digital business models and data security, has in the eyes of some ACs also created the need for additional skills to be brought onto the AC to help it best cope with these new issues. This is, however, a slow process.

The average tenure among AC members in the eight countries analyzed is 5.5 years, with anecdotal evidence implying that the real number across Western Europe is even higher.¹⁹ Thus, to add new skills to an AC and integrate them into AC members' work can be a decade-long process in countries with longer terms for members of supervisory boards and boards of directors, particularly as ACs continue to remain relatively small in size.

This theoretically gives an inherent advantage to firms in countries where the system or culture encourages a more rapid turnover of board, and thus AC, members.

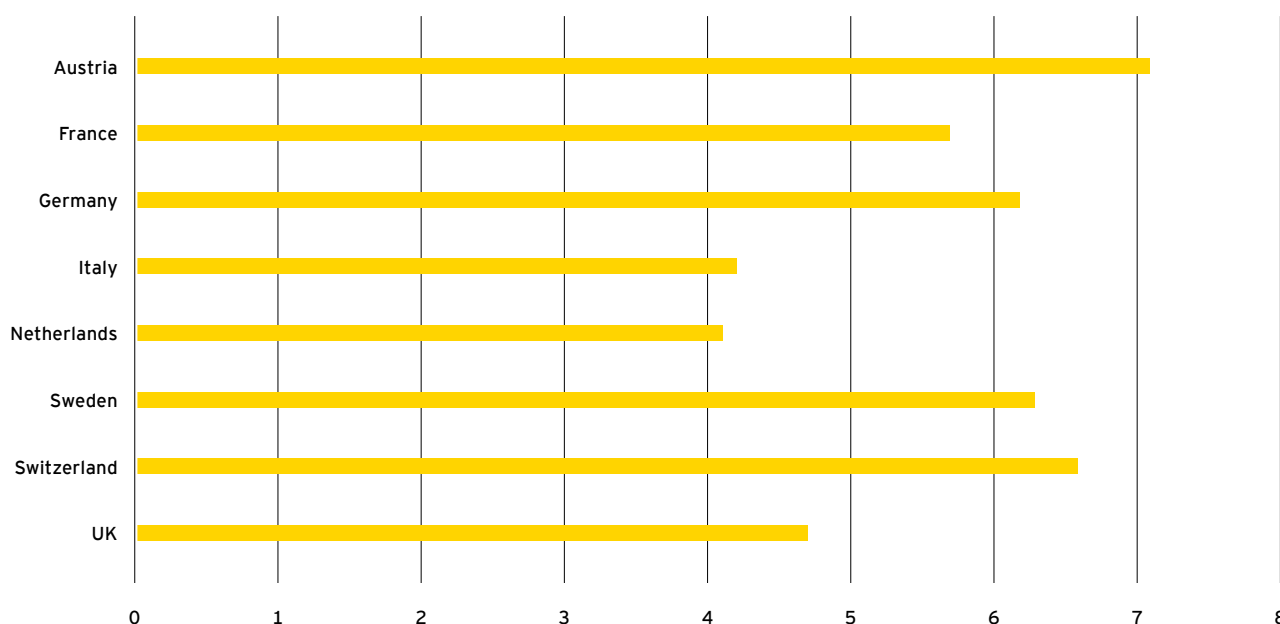
This benefit, however, is not always readily taken advantage of, with rates of AC member turnover, measured as average national tenure divided by the average number of AC seats within a national system, being rather consistent across systems.²⁰ While firms in the UK, Switzerland and Scandinavia each have one-year terms of office for board members before re-election, only in the UK does this appear to have noticeably shortened AC tenure. Germany, which has a maximum board term of five years, experiences slightly more turnover than both Sweden and Switzerland, though this could also be due to its larger AC size – giving it more opportunities to replace members.

What is clear from this, however, is that in every country, board turnover is infrequent. This means that ACs across Europe will struggle to keep up with the pace of change in company risk profiles brought on by digitalization, if they have not already considered the addition of digital skills into their board succession process. It is insufficient for boards and ACs to simply acknowledge the importance of these new skills. Active planning is required to make sure that enough diversity of skills can be integrated into an AC before serious risks emerge.

¹⁹ This figure is the average per AC member across countries. It is not an average of the five country figures. The figure was compiled based upon the average AC member tenure for firms listed on the major national stock index for each country. A full summary of how the data was created can be found in Appendix 1.

²⁰ See Appendix 1 for data on turnover rates.

Figure 3
Average tenure of Audit Committee members (years)



INTERVIEW

INTERVIEW

Simone Menne

Member of the Supervisory Board
at BMW AG



Simone, as a member of a few two-tier supervisory boards, how do you understand your role toward the executive board members in that structure? Would you say it is more about leading management, supervising their work, or being a consultative partner?

In my experience, I would say it is more about supervising the work of management than consulting with them or leading them. Being a member of a two-tier board is mainly about ensuring proper governance, compliance, internal control structures, and risk management. Within the role there is a significant amount of responsibility for providing oversight on mandated governance and compliance tasks.

This means that the role of the supervisory board is more geared toward the board asking questions about the background of these systems within the company, and not so much on providing strategic advice to management or consulting with them on organizational forms.

How about in the setting and execution of company strategy? Do you see any difference there?

Here, the board is somewhat active in the setting of strategy, as we have at least one meeting per year where we discuss the company's strategy at length and ultimately provide our approval on that strategy.

It is important to note, however, that this discussion is more of an advisory role than what the board normally occupies. Now, making this strategy work is not a role for either the supervisory board or the AC, and is instead the responsibility of management. To simplify it, you could say that the supervisory board is consultative in the setting of the company's strategy, and then occupies a more traditional role in supervising its execution by management.

A key theme today surrounding ACs is measuring the quality of the work done by the external auditor. On the audit committees you sit on, how is this done?

This is a very good question. Of course, as an AC we always ask the external auditor about their approach to the audit and the type of controls they have utilized, so that we understand in which areas they have done controls by comparison and in which by algorithms. How many interviews and talks with management and employees have they done? In some areas you can also have a look with other consultants to make sure that the external auditor is not auditing himself or herself. So that is a way of quality measurement.

There is the possibility – but that is just by comparison, as I sit on several boards – that I personally can also compare the quality of auditors reports and can ask the external auditor to provide things I have seen another provide that I thought was good quality. There is also obviously the need to regularly exchange auditors, so that you have the independence of the auditor and an understanding of the quality of the different auditors.

The scope of compliance and financial reporting requirements in Europe has steadily increased in recent years. In your opinion, is this putting too much strain on the ability of the AC to carry out its core capacity, and if so, should some of those responsibilities get shifted to a different part of the supervisory board?

It is funny you ask this, I am just now preparing for an AC meeting and am having to review over 400 pages of material, including three different reports from external auditors, including a risk management report, a year-end closing for the firm, and a document on data privacy and cyber security. This is clearly a wide remit.

While it has never been openly discussed, given the variety of tasks and risks now being considered, I could imagine issues related to the use of technology, data, and cyber security being given to a new expert committee. In the current context, it is a huge workload when you think that we as an AC have to ensure compliance with all of these evolving regulatory issues. It is difficult to handle all this at times and is certainly a new burden on ACs.

Corporate behavior is another issue that has become more visible and a reputational risk for firms. In your opinion, to what extent should the AC be a part or driver of a company's conscience?

I am very much in favor of the AC being a driver of this, and it has not been done enough, as it is quite difficult to properly achieve if you, as an AC, only meet four or eight times a year. Ultimately corporate behavior is about the tone set by the top, and as we, as an AC, are responsible for compliance and the monitoring of fraudulent actions, I think we naturally then become a driver for setting company behavior in those areas. I also think that this will become more of an issue in the future due to some current examples of poor corporate behavior that are in the public consciousness.

Given the changing nature of both audit and traditional business models, what are your expectations toward changes in the skill set of AC members in the coming years?

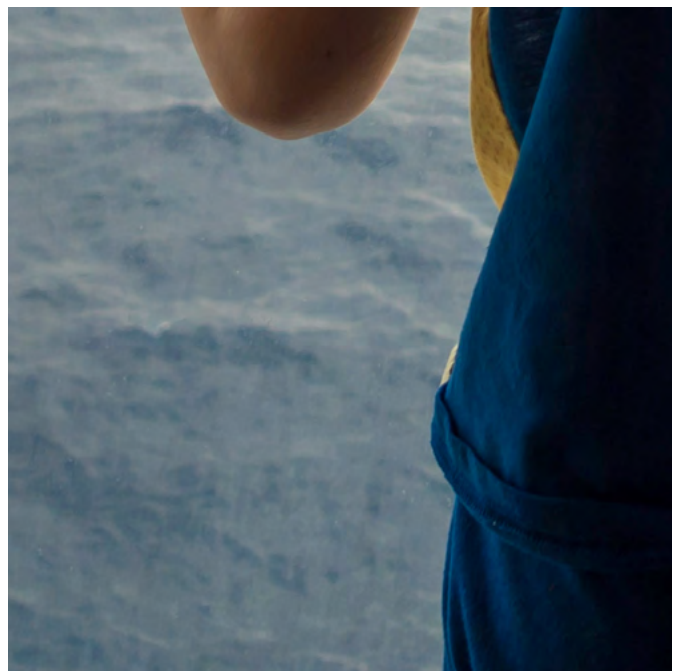
At the moment, the skill set demanded of AC members is vague, in that we just need to be financial experts. But as you see in supervisory boards already, you may ultimately see more diversity in the skill set of the AC. Depending on the firm, there could need to be more expertise in operations within listed companies, in M&A, or in tax. But that very much depends on the portfolio and shape of the company. But I do imagine it will be more precise than just having finance experts, and it would be helpful to have experts on topics such as cyber security and data privacy.

Forward-looking or putting out fires: a difference in current and future outlook



There is a growing divide that exists on what topics make it onto the AC agenda. Discussions with ACs have revealed that two perspectives are generally used to frame the AC agenda: one that is tactical and focused on current business issues or newly enforced legislation, and another that is concerned with emerging trends and issues that could develop over a longer time horizon.

As mentioned before, this divide is not founded in structure. Instead it is the breadth or narrowness of an AC's remit that is the main determining factor, such as the responsibility of Dutch ACs to consider cyber risks and external stakeholders. As a result of this, some systems, such as those in the UK and Italy, which take a narrower view of their role, have markedly different agendas to those of the Netherlands and Sweden, which have a broader scope of responsibilities. Interestingly, firms in France and Germany are divided, with no unifying national trend in their AC agendas. These different perspectives on the role of an AC impact not only their current work but also their future outlook.



Tactical concerns are the dominant agenda item

For firms in the UK and Italy, as well as some in Germany and France, the tactical approach to the agenda and to issue management is the dominant approach. While the exact agenda items vary strongly by industry, geography and firm, with some focusing on issues such as a net asset value report or responding to new International Financial Reporting Standards, the common factor is that the AC agenda is dominated by activities related to solving or mitigating an immediate issue of the firm. This issue is almost always related to the traditional tasks of an AC, such as financial reporting and compliance.

Some audit committees take a different approach

Some ACs, particularly those in the Netherlands, are less concerned with the tactical issues and the traditional financial back casting work of ACs and are seeing their agendas more dominated by emerging risk issues and making sure the business is adequately prepared to handle change. Topics that frequently appear on AC agendas for firms with this outlook include: cyber security and data, digitalization, improved audit quality, and external factors such as climate change and business model development.

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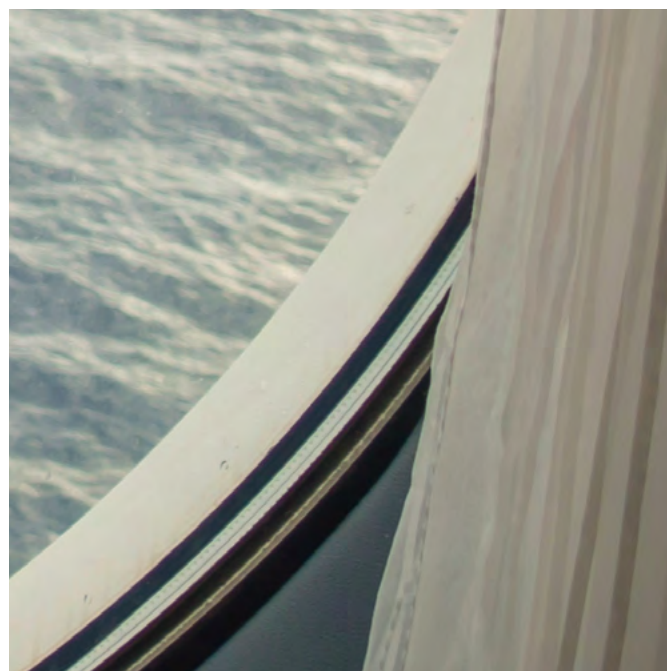
Audit committees that have expanded responsibilities are more likely to take a forward-looking approach to their work.

Divide on which skills will enable success

This division on the AC agenda cascades into how ACs view their role going forward and the skill sets they need to fulfill that role successfully. While ACs in every country acknowledge the importance of having individuals with financial skills on the committee, particularly for the AC chairperson, as well as prior executive experience, those that focus on tactical concerns do not believe additional skills are required. Instead, they feel that the skill sets that currently exist on ACs are by and large capable of handling the tasks of the committee, and that when issues arise that require different skill sets, outside experts can be brought in to help guide the AC or board as needed.

This differs strongly from ACs with a more forward-looking perspective, where the need to add expertise in digital technologies and compliance issues is widely recognized and increasingly planned for.

This split in outlook and on the corresponding need for digital skills shows a clear divide over the structural importance of digital skills and the impact that digital tools will have on the business areas overseen by ACs. Those ACs in systems with a narrower remit are significantly less prepared to handle digital risks compared with others.



Handling changes in regulation and increased responsibility

Nonetheless, AC members across systems and countries are relatively united in their belief that although the tasks assigned to ACs have, and will continue to grow, the responsibilities of the AC should not be divided and given to an additional committee. Although wary of the growing impact of regulation on their work, ACs outside of the financial services sector, which has already widely adopted a separate risk committee framework, largely remain convinced that they are still the best-positioned to handle audit, compliance and risk issues, as the topics are too interlinked to be divided effectively.

Helping foster a good “corporate conscience”

Corporate behavior and reputational risks also seem to be a topic of increasing importance for boards overall, as well as ACs, as financial reporting and the internal control process serve as strong public indicators of how a company behaves.

To this end, the role of the AC as forming a part of the company ‘conscience’ is growing in importance for AC members. While the responsibility for this is seen as being that of the board of directors or supervisory board, as well as that of senior management, AC members increasingly feel that the work of their committee is a part of the process and helps shape positive corporate behavior.



Audit Committees can help shape positive corporate behavior.

Examining national differences in Audit Committee development

As is clear from their view on their own future needs and current obligations, ACs within Europe have developed different characteristics to their work as well as to their structure. This produces an asymmetry, where the work of one AC is not necessarily the same as the work of another.

Yet, in an environment where business partners and investors need to increasingly understand how ACs view their work and role, being able to effectively compare national systems is increasingly important.

The following infographics are designed to help provide that comparison, helping to visualize both the structural differences between ACs as well as their different current roles and views on digital skills.

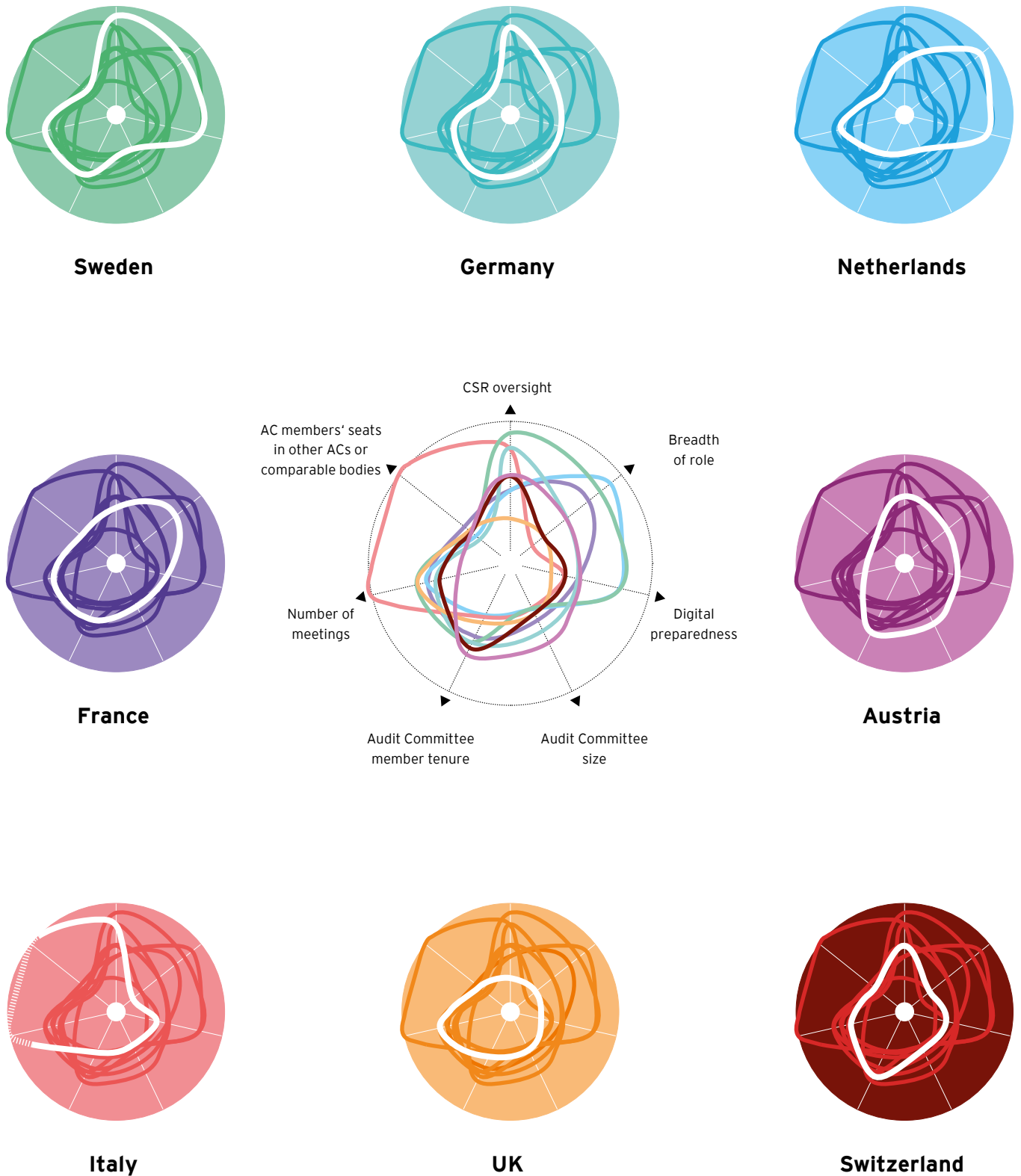
With qualitative rankings demonstrating on a 1 to 10 scale how active ACs currently are in overseeing CSR reporting, the breadth of their current activities (with breadth gauged as beyond a pure financial focus), as well as their preparedness to handle digital risks, the current work of ACs relative to each other is assessed. Along with this qualitative information, quantitative data on AC structure, level of activity of ACs and their members has also been included, providing an overview of ACs structural underpinnings and an assessment of how the role is currently prepared for or engaged in future oriented tasks.

The data set used to create these graphics was compiled through a combination of qualitative analysis of the 20 interviews conducted by Oxford Analytica with AC members, research into the work of ACs in each country, and quantitative data on AC tenure, size, meeting frequency, and additional AC roles compiled from firms listed on the major stock indices of Austria, Germany, France, Italy, the Netherlands, Sweden, Switzerland and the UK.²¹



²¹ Additional information on the data set used to create these graphics, how it was compiled, and what it contains can be found in Appendix 1.

Figure 4
A comparative analysis of audit committees across Europe
 (white line = respective country; colored lines = all other countries)



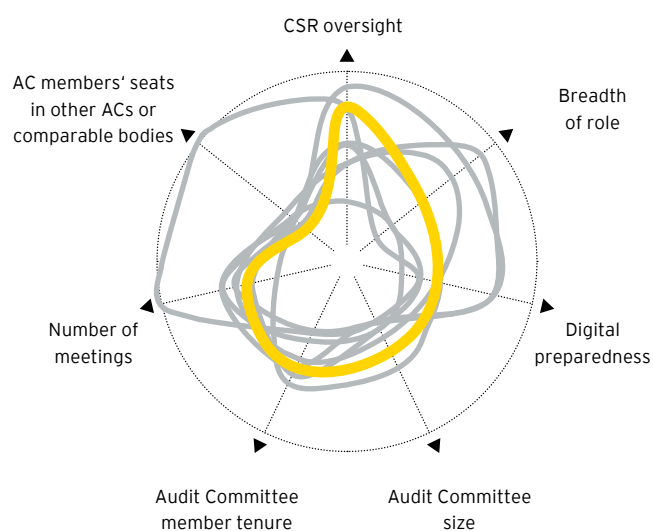
The unique governance rules for Collegio Sindacale and their membership provide for an unusually high number of meetings and a small pool of qualified members.

In-depth analysis: a look at the GSA region

Germany

Due to their larger than average size, relatively high rate of turnover, and high degree of involvement in overseeing CSR reporting, German ACs are relatively well prepared for the changes coming to ACs and risk management. A high amount of capacity for additional tasks and the ability to add new skills quickly as they become increasingly important to the work of ACs will help ensure that the role of German ACs only grows in importance. Where German ACs can improve is in encouraging a more active role for the committee in terms of evaluating risk, and in preparing for the impact of emerging technologies.

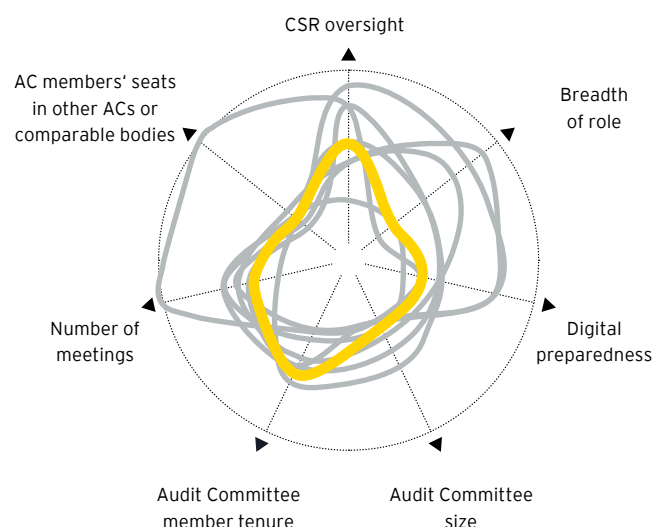
Figure 5



Switzerland

The performance of Swiss ACs is tied strongly to their relatively constrained role, which limits them from being as actively engaged in forward-looking risk issues as ACs in other countries. While this has negatively impacted their performance on digital preparedness and the breadth of their role, the increasing use of integrated financial reporting in Switzerland means that Swiss ACs are becoming increasingly involved in overseeing CSR work, which often involves the work of an external auditor. This trend is a relative strength for Swiss ACs and will help enhance their role in oversight of non-financial reports.

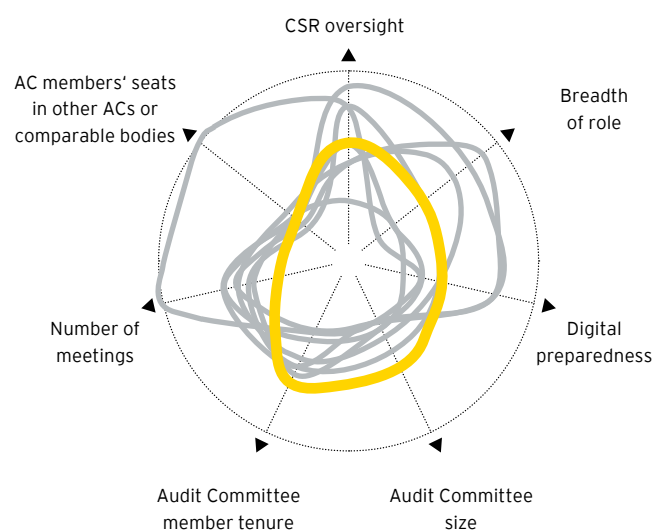
Figure 6



Austria

Austrian ACs perform comparably well both in their capacity to handle new tasks and the breadth of their role, which is less restrictive than in Germany or Switzerland. This means that there is substantial room and capability for growth on the part of Austrian ACs, which have the human capacity to take advantage of their larger remit to be more active in areas where they are currently more hands-off, such as CSR reporting, which remains the responsibility of management.²² The challenge facing Austrian companies and ACs, and where they are most able to improve, is in their potential to upskill and add new competencies to the AC.

Figure 7



22 Austrian Code of Corporate Governance, January 2018.

INTERVIEW

INTERVIEW

Leen Paape

Chairman, Nyenrode Corporate Governance Institute



Leen, as a member of a few two-tier supervisory boards in the Netherlands, how do you understand your role toward the executive board members in that structure? Would you say it is more about leading management, supervising their work, or being a consultative partner?

In my opinion our relationship toward the executive board members is gradually shifting over time. Within the two-tier system the role is to supervise the executive, yet if you look at what is happening in practice over the last few years, you see that while the executive is still in charge of strategy, the supervisory board has become more closely involved in that process, making it a more collaborative body.

This is particularly true when we examine the role the supervisory board plays in the setting of the firm's strategy. In the past, it could be described as an 80/20 split, with 80% of the focus on execution and 20% on the future orientation of the business. Nowadays, due to changing rules and regulations and the fact that members of the supervisory board are all aware that business models are changing rapidly, this focus has changed - there is a need to be aware. So, from a risk perspective, my answer to the executive board is that strategy is also my domain, in that it needs to be done in close concert with the supervisory board so that we do more than just reviewing or marginally assessing it. This is necessary, as if you have a bad business model then there is a significant risk that the company is at jeopardy.

This means that today, I think supervisory boards, particularly in the finance industry, operate more along the lines of a 50-50 model, where we are split between setting the company's strategy and supervising that the executive board achieves that strategy.

I would personally prefer that it shifted even further toward 40% execution and 60% forward-looking, but 50-50 is a good balance at the moment.

A key theme today surrounding audit committees is measuring the quality of the work done by the external auditor. How have your audit committees gone about doing this and are you satisfied with the way audit quality is currently measured?

This is a difficult topic, and I have even done some research on this in an academic capacity.

The reality is that I am unsure if the current proxies for audit quality are really good ones to use. At the moment we focus on topics such as how many restatements there were or if there were any significant deficiencies. I am however not sure if those are truly good measures of audit quality. But for measuring quality, it all starts with the individual in charge of the external audit, as you have to get a sense of their competence and their experience in the industry.

If you were to ask me for a set list of criteria, I can't give it to you. What I can say is that it is a matter of who is in charge, how they interacted with the company and the supervisory board, their experience, and the changes in the external audit team.

To be frank, this is a difficult but important topic, and I don't think audit firms are currently living up to my expectations. I always tell them I would like to see that they have a broad perspective and don't just focus on financial reporting. To me, a strong external audit should take a broad view and spend time within the firm in non-financial areas. Currently, the external auditor is kept more and more in the boundaries of reliability and financial reporting, which is good in and of itself, but no time is then left and no incentive in place for the external auditor to take a wider view of the firm and to have team members with non-audit experience that can evaluate the company as a whole. This is something that I would like to change.

Another emerging theme for audit committees has been the growing importance of Corporate Social Responsibility reporting. How are these statements looked after in the Netherlands and are you satisfied with this process?

Where I am involved, the CSR report and the financial report is often integrated into a single document, so that we don't have to separate statements. Ultimately, this is done so that we can have a uniform view of the entire firm. Despite being in the same report as the financial

statement, it is important to note however that the CSR statements are not being audited. That is something I would like to have changed. To me, if it is an important statement it should be audited. Another important distinction to make about any auditor statements for CSR reports is that when the largest companies report on CSR, and have an auditor statement, it is always a negative one, meaning that the auditor is simply saying that they haven't been able to identify any conflicting statements, it doesn't in fact confirm the information within the report. That is not what it should be. It should be a thorough process, with a positive audit confirming the claims of the company, but that is a work in process.

Looking ahead, what issues do you think will dominate the Audit Committee agenda?

Well in 2018, the most important issues for us as an Audit Committee were combining risk and return, and examining the risks associated with our current business model and how that can withstand competition from innovative entrants to the market. But looking forward, we are thinking hard about the possible impact of climate change on the business, technological innovations and their impact on the business model of the firm, and new incumbents in the industry. I think for us going forward more and more time will be spent on thinking about how we can be innovative and what we can then do to help with the execution of that strategy.

As an AC member, I have already seen what the firm has done over the past 5-10 years, and I am confident that we have adequate control over what we already do, so these topics are not a significant concern to me. But the future is far less certain, so to me, we have to focus on the risks that those changes represent, and I duly expect those issues to dominate the agenda of ACs going forward.



Where does the Audit Committee go from here?

Given the divide that exists among European ACs in outlook and the absence of best practices in other areas, a key question that needs to be asked is where do ACs go next, and what can be done to help best prepare them for upcoming changes in AC responsibility and the increased demands of the role?

The areas where the most impact can be made are: solving differences in the oversight of CSR statements and the understanding of digital technologies and their importance; creating more standardized guidelines for AC member tenure; and increasing AC interaction with regulators and policy makers.

CSR reporting – enhanced oversight and the creation of a positive audit standard

An area where the role of the AC is already emerging is that of CSR reporting.

While reviewing and approving company CSR statements has increasingly become an area of AC responsibility, this needs to be further solidified and codified into national codes of corporate governance. As CSR presents not only a reputational risk to a business, but also represents a component of its operational and financial transactions, it should become a standard part of an AC's duties to assist the board of directors or supervisory board by reviewing and auditing these statements as part of their normal workflow, as they do for financial accounts.

In creating this standard practice among ACs, the means by which CSR statements are audited should also be brought into line with best practice, and a positive audit of firm activities undertaken. While present in the CSR reports of some firms, all too often the audits of CSR statements are done to a negative standard. This finding only of no major errors or omissions provides relatively little assurance about the true accuracy of CSR statements, diminishing their value. As ACs become increasingly involved in the review of CSR reports, the establishment of guidelines serving as a basis to provide an audit opinion as compared with a review opinion, similar to what is done for financial reporting, should be of primary importance.

Recognizing the importance of digitalization and the changing nature of audit

CSR reporting is increasingly seen by ACs as an area where they can grow in responsibility and take ownership. However, ACs remain fundamentally divided on how they interpret the importance of digitalization and the new digital tools that will not only reshape internal business functions but will also fundamentally alter both the internal and external audit processes. While some AC members believe that sufficient knowledge of these developments and the risks they create can be provided on an ad hoc basis by external subject matter experts, this solution to the problem does the AC a disservice, by making it reliant on external knowledge for oversight of what will be, and increasingly already is, an important aspect of their work.

It is thus important for ACs to acknowledge the substantial business and reputational risks posed by the advancement of digital tools, and that understanding of these risks goes beyond the traditional financial and accounting skills currently anchoring the traits of the AC. There should thus be a steady demand for the introduction of individuals with these skills into the AC, so that they are best prepared to undertake the tasks associated with the future casting they are already doing. Bringing these skills into the AC will also increase the ability of the committee to audit the use and investment by the firm into new financial tools and processes and compare that to competitor and partner firms. This will help to enhance overall firm resilience and ensure that significant pushback can be given to management on decisions relating to the purchase or use of new technologies.

“

Digital tools and business models will change the nature of financial audits.

Audit Committee tenure – a solution to the problem of changing skill sets?

With external expertise not sufficient for ACs to handle the changing nature of audit and the risks presented by the growth of digital processes and tools, ACs must work harder to add critical digital skills to their ranks. This is, however, currently a slow development and one that has been described as potentially a decade-long process, due to the length of terms for supervisory boards' and board of directors' members. This makes the task of upskilling board committees such as the AC a difficult one.

The solutions to this are straightforward in that both ACs and supervisory boards/boards of directors can be expanded to accommodate additional members who have this new skill set, or the terms of board members can be shortened, or limits placed on their renewal, helping to encourage and increase AC member turnover. As supervisory boards and boards of directors have consistently shrunk in size over recent years, reversing that trend to accommodate digital skills is unlikely. Thus, the latter options, such as shortening board terms or capping their renewal, are the easiest and most straightforward means of fostering higher rates of turnover, which can help bring additional skills onto the AC.

Although perhaps uncomfortable for some AC members – and not without some risk, as new members may be less familiar with the firm, its business model and risk profile – the need to add digital skills to the committee is nonetheless a pressing concern, and thus significant changes to AC membership are required. ACs such as those in Austria, where AC members serve on average over seven years, should re-evaluate the length of board terms or their ability for renewal, and in doing so, develop a timeline for the addition of new skills to the board. Additionally, organizations that produce corporate governance codes, should also re-evaluate board tenure, and develop guidelines that make it easier to bring new skills into the boardroom, and include the addition of these skills into guidance on board succession planning.

Becoming more public-facing – engaging with external actors

The inability, due to legal requirements, or hesitancy of ACs to engage with some external stakeholders such as investor groups and financial analysts is understandable. This means that the minimal contact between that set of actors is not controversial or harmful to the AC. However, the reliance on informal dialogue between ACs and regulators is more problematic.

The lack of a regular process by which ACs can communicate with regulators and policy makers is potentially an obstacle to effective stakeholder communication. Although AC members and Chairs seem satisfied with the informal communication that currently takes place, as the degree of regulation that impacts the work of ACs will only increase throughout Europe in both the short and medium term, the demands for clearer communication will increase.

ACs should therefore consider developing mechanisms by which they can more formally and systematically share their own concerns and vantage points with regulators and policy makers, so that they can have a more impactful voice on future regulatory decisions. This would also help to better prepare them for the already quickening pace of regulatory change.

“

More steady and formal engagement with regulators and policy makers can help keep ACs from being overwhelmed by regulatory change.



Conclusion – keeping audit committees fit for purpose

This examination of ACs across different European geographies has revealed that as a result of the varied board structures in place and the uncertain nature of the transition currently facing ACs, a series of perspectives on the current work and future role of ACs exist. These differing perspectives and views on the role of ACs, along with the presence of less-defined tasks, has created the need for additional best practices and an increased common understanding of the future role of the AC.

Structural differences less important than scope and understanding of responsibilities

The genesis of this difference in outlook between ACs initially lies in the diverse board structures in use, the varying breadth of AC responsibilities, and the resulting size and activity level of ACs. With the presence of both one- and two-tier board systems, ACs in Europe have varying degrees of closeness with management and independence, as well as in their delineated tasks. Although European ACs fluctuate in size along with the frequency of when they meet, it is ultimately the differences in scope of AC responsibilities and their interpretation of their less explicitly-defined tasks that have the most telling impact on how ACs view their role and how it may shift.

ACs with a narrow financial remit and composed of individuals with mainly financial expertise such as those in the UK, Switzerland and Italy are currently fundamentally more likely to take a more closed view of both their current tasks, as well as how those tasks could change in the future. By contrast, companies in the Netherlands and Sweden, which take a broader view of the role of the AC, are much more likely to be concerned about emerging risks and orient their agenda to consider those issues.

Helping audit committees embrace tomorrow's challenges

The key task for ACs in the immediate future is therefore to bridge this divide, and make sure that they maintain a balance between today's operational and reporting challenges and being properly prepared for tomorrow's unseen risks.

To accomplish this task, and therefore stay fit for purpose, European ACs need to:

- ▶ establish a clear best practice for their involvement in overseeing CSR reporting as well as clear guidelines as a basis to provide an audit opinion as compared with a review opinion;
- ▶ acknowledge the need to add skills relevant to the digital tools, processes and systems impacting internal business functions and the role of internal and external audit;
- ▶ consider adjusting board committee tenure to help bring those new skills into the AC more quickly; and
- ▶ engage more openly and formally with regulators and policy makers.

In accomplishing these four tasks, ACs can help ensure that they are prepared to handle the additional responsibilities that are being increasingly asked of them, respond to and prepare for changes in company risk profiles, and increase external trust in their traditional role, which is the approval of financial accounts.

Changing nature of audit – keeping audit committees prepared for the future

ACs must also look further ahead and prepare for how their traditional role of evaluating historical financial information will also change with the advent of new technologies. This means going beyond the changes and needs that can be seen and acted upon but anticipating those that will have a more transformative impact on audit as an industry and as a component of financial accounting.

With the advancement of data analytics, predictive modeling, and artificial intelligence, the internal and external audit processes, as well as the system of internal controls, will be increasingly altered from a process that relies now on human knowledge and skill, to one that can become digitized and automated, reducing the potential for human error. Understanding and preparing for how these tools will shape not only the audit process, but also the way it is reviewed, will be critical to ensuring that ACs remain fit for purpose over the next 5-10 years.

The task of ACs in Europe is therefore not only to stay current regarding the risks it can see on the horizon, but to prepare itself for the coming impact of digitalization and Industry 4.0 on the audit process.



Appendix



48 **Appendix 1:** Data overview and methodology

52 **Appendix 2:** Works cited

Appendix 1:

Data overview and methodology

To conduct quantitative analysis of audit committees in the eight countries covered within the report (Austria, France, Germany, Italy, Netherlands, Sweden, Switzerland and the UK), data was collected from a sample of firms listed on the major stock indices of each country. These were: ATX (Austria), CAC 40 (France), DAX 30 (Germany), FTSE MIB (Italy), AEX (Netherlands), OMX 30 (Sweden), SMI (Switzerland) and the FTSE 100 (UK).

For France, Germany, Italy, Switzerland and the UK, data was collected from 30 companies on each stock index, while for Austria, Sweden and the Netherlands data was obtained from 20 companies. For each company, the following categories of data were taken from their annual or corporate governance reports, either from the year 2017 or 2018, whichever was most recently published at the time of collection (December 2018 – January 2019).

- ▶ Size of AC
- ▶ Average tenure of AC members (in years)
- ▶ AC members' seats on other companies' boards
- ▶ Number of regular meetings of the AC
- ▶ AC members' seats on other companies' AC or comparable bodies

This data was then compiled to form country averages. The below table shows the figures that were calculated.

Figure 8

	AC size	AC members' seats on other companies' boards	AC members' seats on other companies' AC or comparable bodies	Average tenure of AC members (years)	Regular meetings of the AC
Germany	5.3	8.3	2.5	6.2	5.2
Switzerland	4.0	10.6	3.4	6.6	5.0
Austria	6.3	7.9	3.2	7.1	3.6
Sweden	3.5	9.6	3.3	6.3	6.6
UK	4.0	8.0	3.6	4.7	6.5
France	4.5	14.3	4.0	5.7	5.8
Netherlands	3.6	9.9	2.9	4.1	6.0
Italy	3.5	17.6	16.0	4.2	19.5



Numerical representation of data within infographic

Figure 10

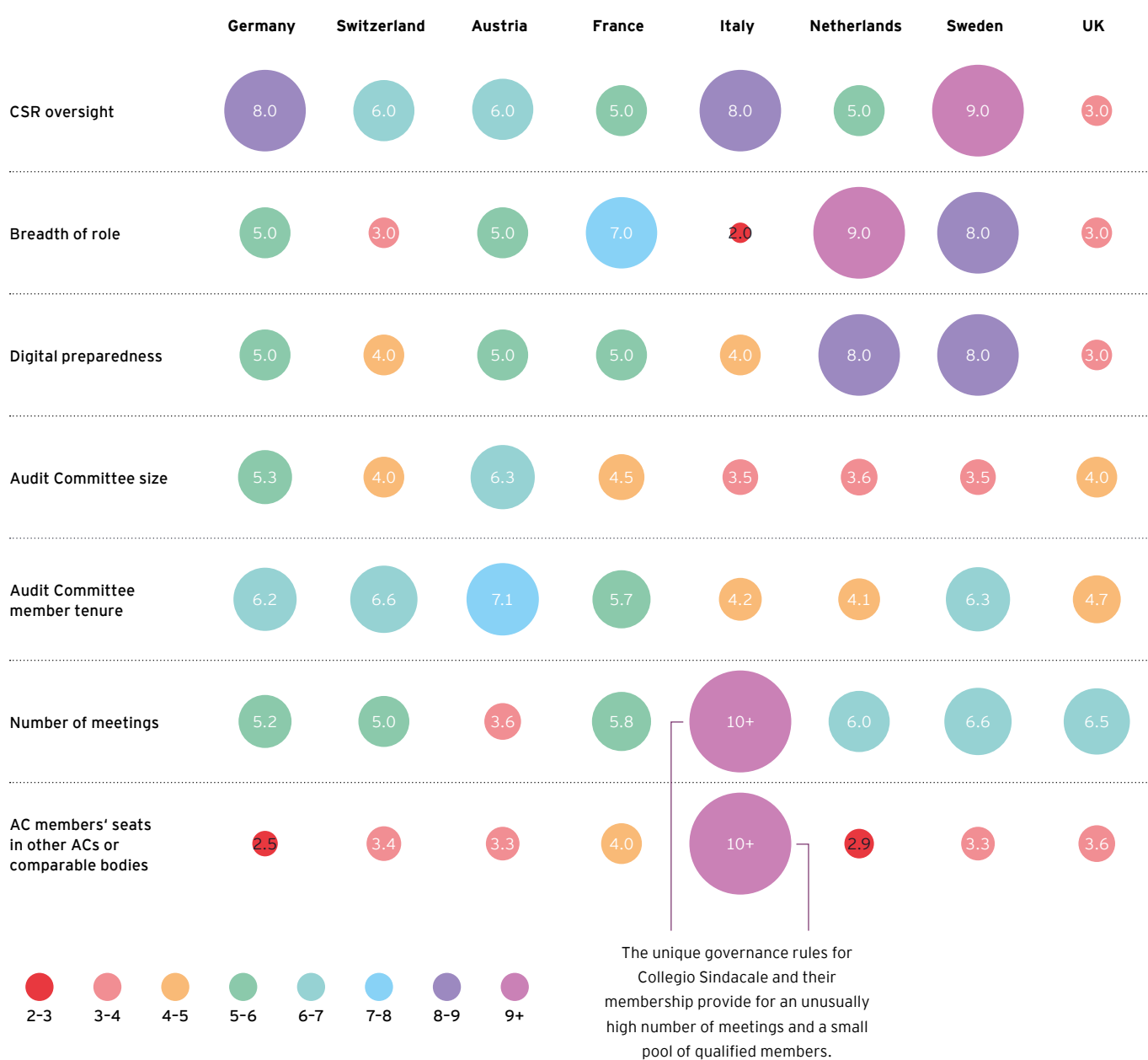
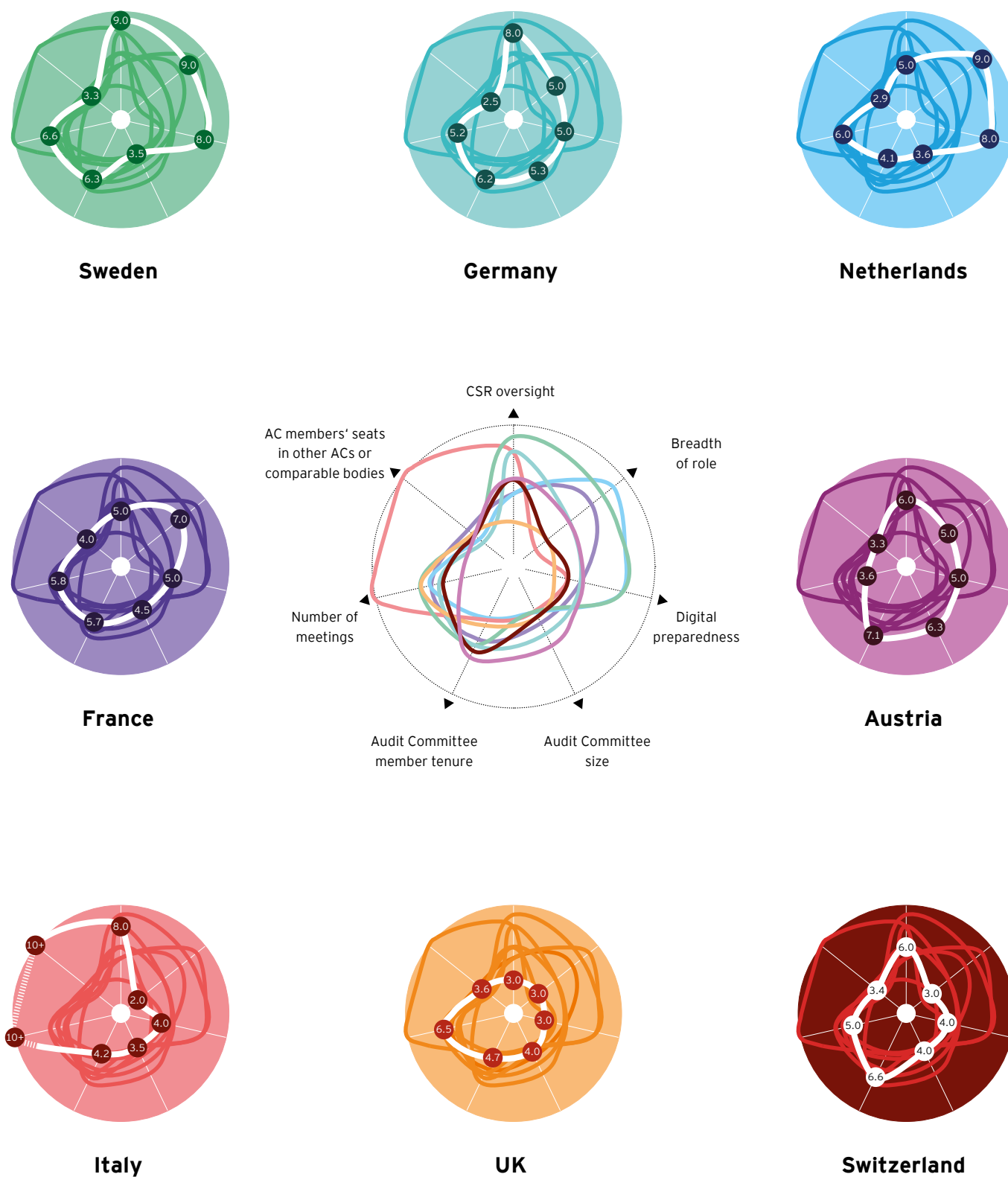


Figure 11
A quantitative analysis of audit committees across Europe



The unique governance rules for Collegio Sindacale and their membership provide for an unusually high number of meetings and a small pool of qualified members.

Appendix 2:

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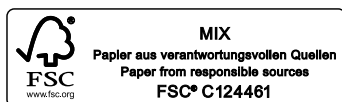
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