



cutting through complexity

The Audit Committee Agenda 2015

Bermuda ACI Roundtable

October 27 & 28 2014





cutting through complexity

Corporate Governance & Hot Topics

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Corporate Governance & Hot Topics



- Recent Corporate Governance Surveys
- Hot Topics
 - ✓ Reassessing the Audit Committee's Role in Risk Oversight
 - ✓ Cyber Security
 - ✓ Investor Activism
- Accounting & Auditing Priorities
- Appendix
 - ✓ KPMG's Audit Committee Priorities for 2014



Recent Corporate Governance Surveys

Recent Corporate Governance Surveys



NACD 2013 - 2014 Public Company Governance Survey

- Annual survey of public company directors
- Provides data on board governance trends and practices
- 1,000 respondents

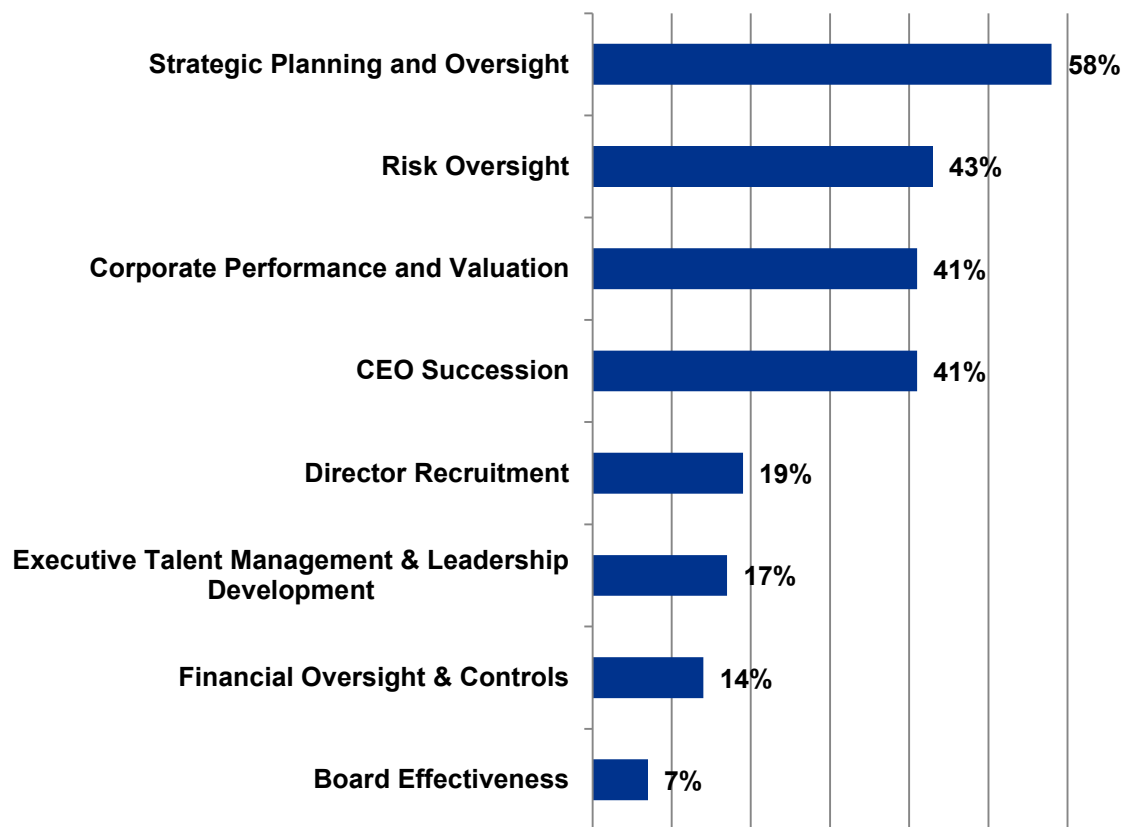
KPMG's 2014 Global Audit Committee Survey

- Annual survey of audit committee members around the world
- Captures views on range of challenges facing audit committees, their boards and businesses
- 1,500 respondents (490 US respondents)

Public Company Governance Survey - Leading Issues



What three governance issues are the highest priority for your board in 2013? (select three)

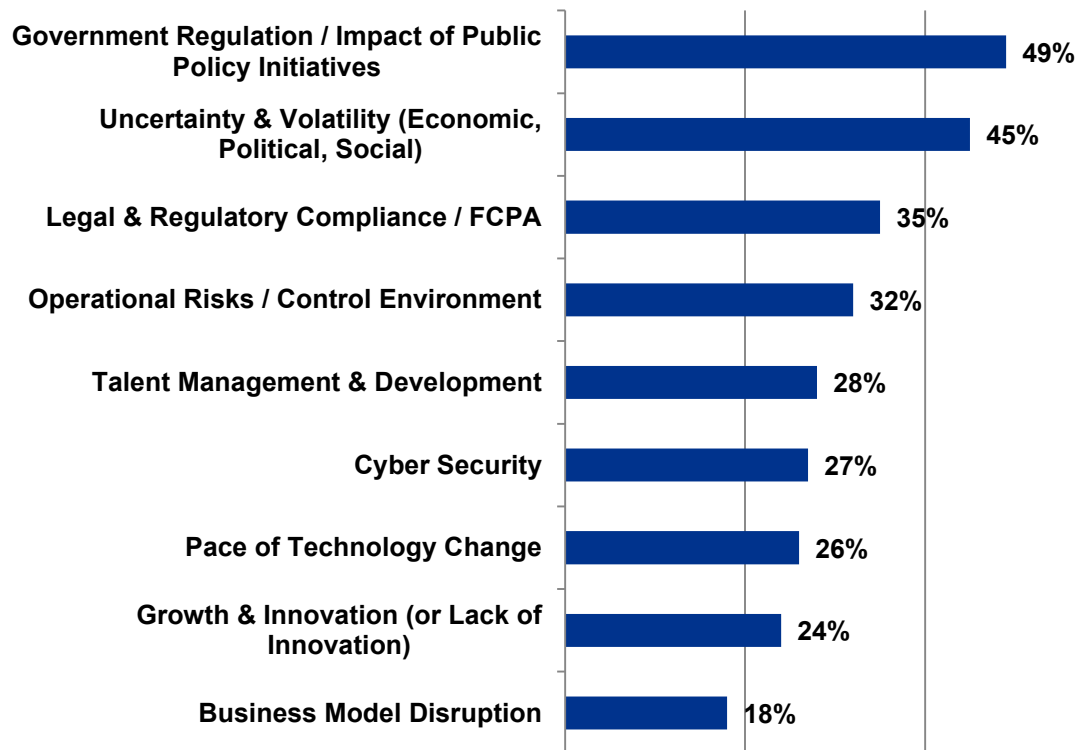


Responses of larger public company directors

KPMG's Global Survey – Biggest Challenges



From your perspective as an audit committee member, what risks (aside from financial reporting) pose the greatest challenges for your company? (select three)



KPMG's Global Survey – Other Hot Spots

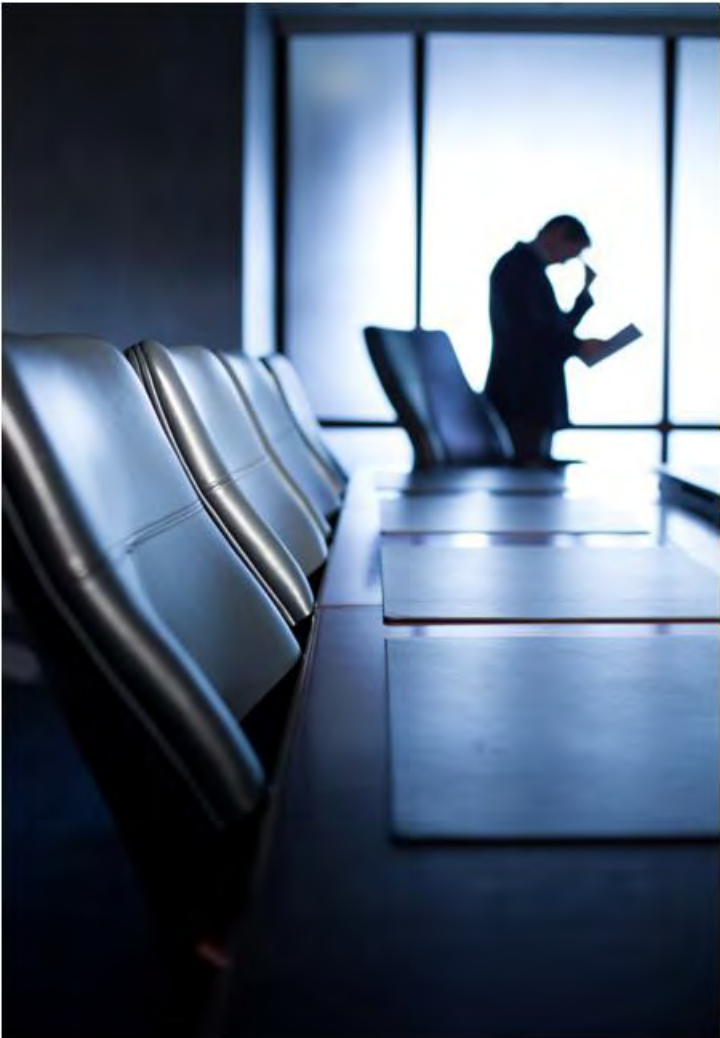


- Succession plan for CFO and talent development of the finance team
- Identification of “leading” versus “lagging” indicators
- Quality of information regarding emerging technologies, from an “offensive” and “defensive” perspective
- Robust, ongoing evaluation of the external auditor with a focus on independence, objectivity and professional skepticism
- Clarity of internal audit’s role and responsibilities (and adequacy of skills / resources)



Reassessing the Audit Committee's Role in Risk Oversight

Risk Oversight – Reassessing the Audit Committee's Role

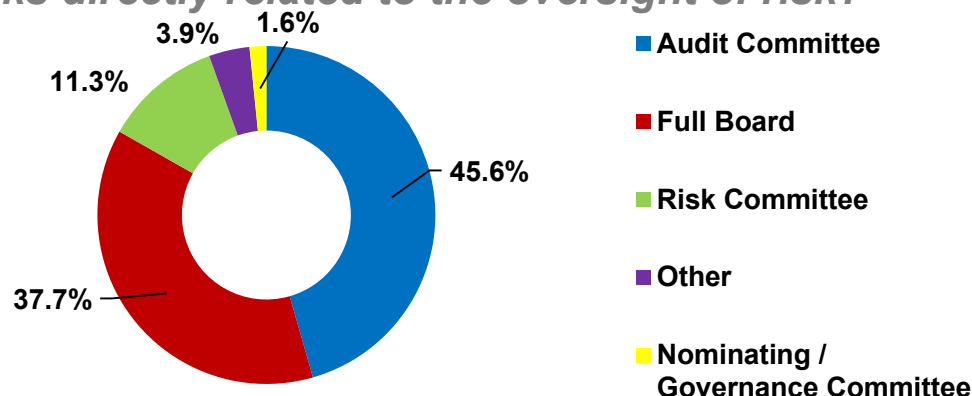


- Primary responsibility for risk shifting to full board
- Each committee responsible for overseeing risks inherent in its area of oversight
- Audit committee's focus often narrowing to risks within the committee's core areas of oversight
- Audit committee uniquely positioned to be a catalyst

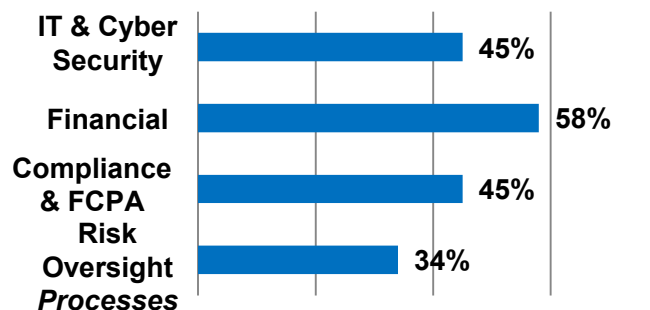
Risk Oversight – Allocations and Focus



To which group has the board assigned the majority of tasks directly related to the oversight of risk?



Aside from financial reporting risk, for which of the following categories of risk does your audit committee have primary responsibility?

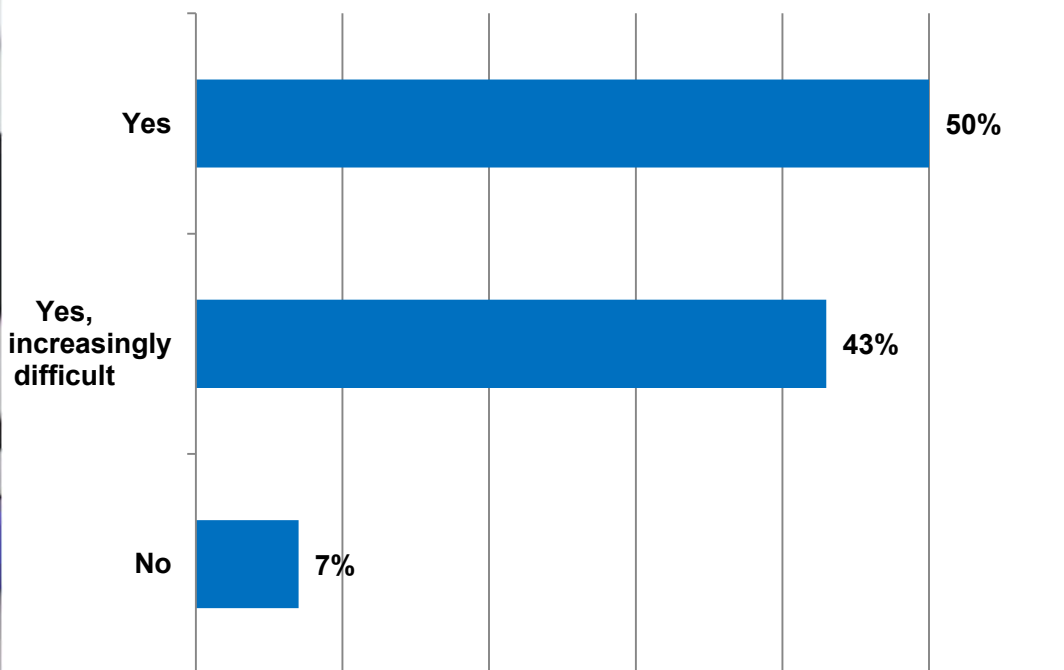


Risk Oversight

– The Audit Committee's Workload & Agenda



Are you satisfied that your audit committee has the time and expertise to oversee the major risks on its agenda in addition to carrying out its core oversight responsibilities?



Is the Board Recalibrating?



- Have board governance and oversight processes changed – and advanced – as the business and risk environment has become more complex?
- Do we have the right people – who understand the business and are willing/able to ask the right questions?
- Is it realistic to assume that the audit committee has the time and expertise to take on oversight responsibility for compliance, cyber and technology risks, and operational risks and controls?
- Is there a need for an additional committee – such as a finance committee, risk committee, technology committee, or a compliance committee?

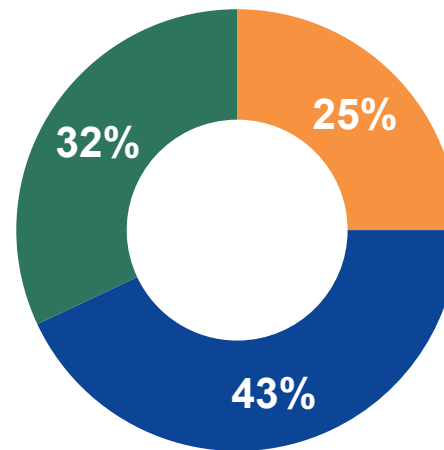


Cyber Security

Quality of Cyber Security Information



Please rate the quality of the information you receive about cyber security – including data privacy and the protection of intellectual property



Good

Generally good-but
issues arise
periodically

Needs improvement

Communicating with the Board About Cyber Security

– Key Areas of Focus



- Cyber security assessment
- Structure of governance around cyber security and how it fits into the company's overall ERM program
 - ✓ Greatest risks to the company's highest value assets – and how human capital and financial capital are aligned around them
- Cyber security "scorecard" – addressing key risks areas, incidents, trending, and what's happening in the environment
- Cyber-incident response plan – defining the processes and steps for managing a cyber incident

Oversight of Cyber Security – Considerations for the Board



- All data is not equal – understand the value of the company's various data sets, and whether appropriate resources are devoted to securing the most critical assets
- Recognize that most IT risk is people risk. How are we monitoring people risks?
- Request regular cyber incident reports to monitor cyber attacks and trends
- Understand the company's cyber-incident response plan
- Conduct robust IT risk assessments periodically – and consider the need for an independent risk assessment



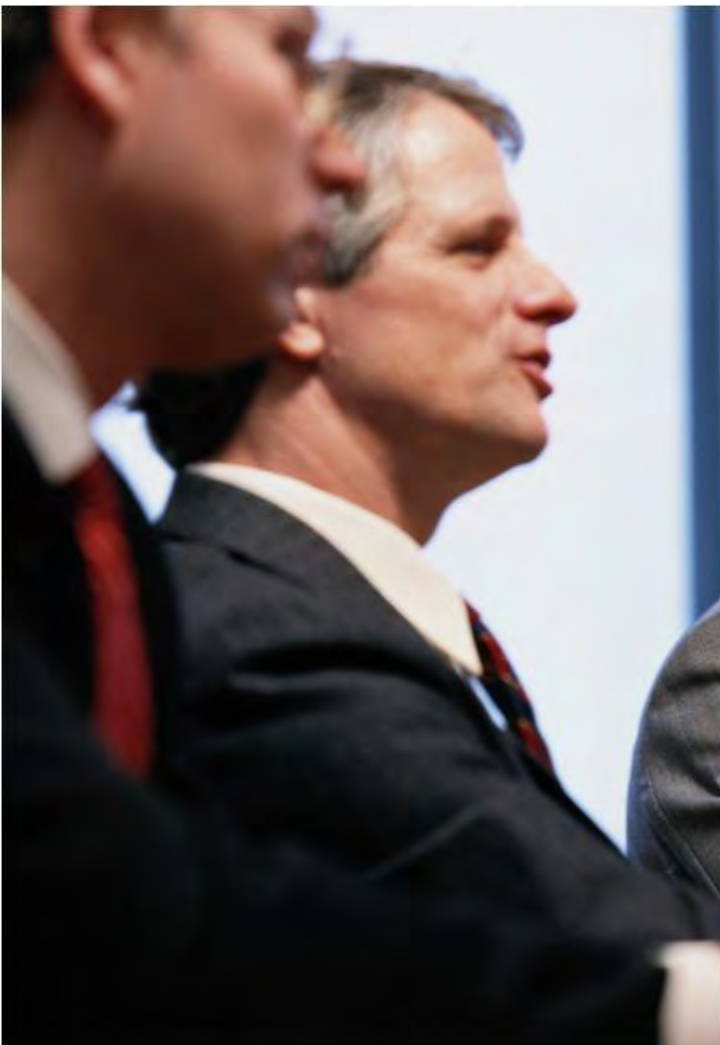
Investor Activism

Activist Investors Include...



- Activist hedge funds (\$100 billion+ in assets)
- Large pension / institutional funds and asset managers, who
 - ✓ Allocate capital to activist hedge funds
 - ✓ Publicly team with the funds
 - ✓ Conduct their own activist agendas
- Socially responsible investment funds
- Individual investors with strong personal beliefs

What Do Activists Care About?

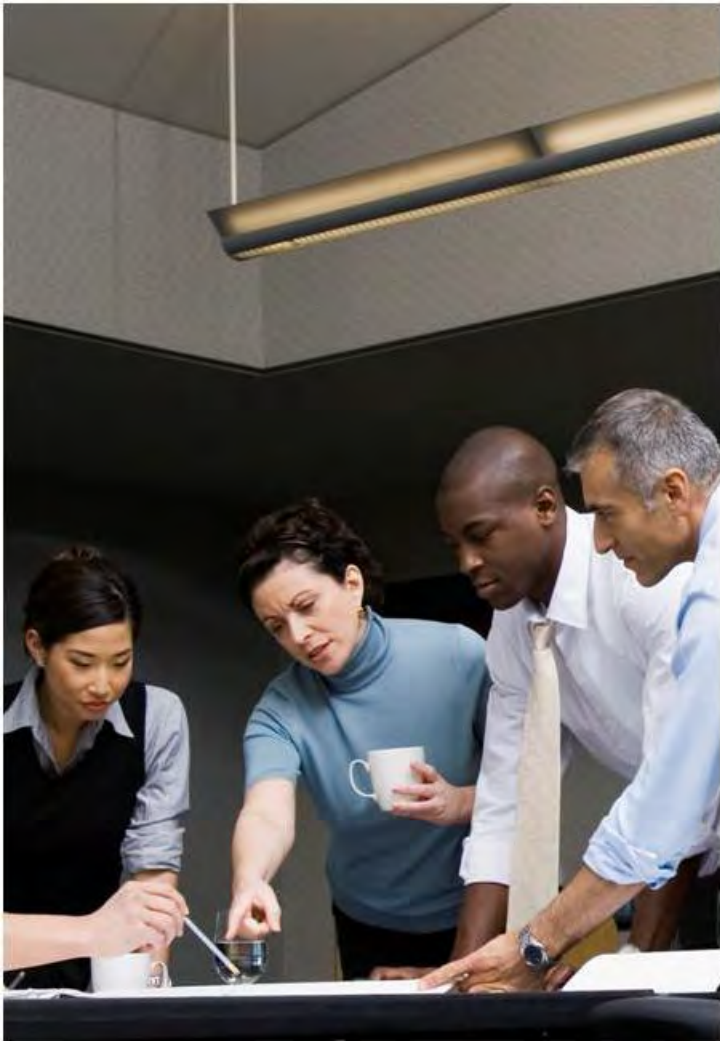


- Strategic / operational improvements
 - ✓ Changes to strategy
 - ✓ M&A
 - ✓ Capital structure
 - ✓ Dividends and buybacks
 - ✓ Management changes

- Governance
 - ✓ Board election & composition
 - ✓ Shareholder rights
 - ✓ Compensation

- Environmental, social, and political agendas

Preparing for Activism



- “Think like an activist.”
- Understand and assess vulnerabilities – Are we a potential activist target?
 - ✓ Stock price
 - ✓ Board
 - ✓ Management
 - ✓ Balance sheet
 - ✓ Operations and strategy
- Address performance gaps
- Know and engage with your largest shareholders
 - ✓ Understand their perspectives
 - ✓ Communicate the company’s position
- Assemble a team to develop a game plan for dealing with activists

Responding to and Dealing with Activists



- “It’s an art, not a science.”
- Considerations:
 - ✓ What does the activist want?
 - ✓ Do they have a point?
 - ✓ What are their tactics?
 - ✓ Role of management versus board
 - ✓ Views of company’s other investors and proxy advisory firms
- Communications strategy – including social media
- Be prepared for a fight – and what that entails

Board / Shareholder Communications: Key Considerations



- When should directors get involved?
 - ✓ Which directors?
- How should directors engage?
 - ✓ With which shareholders?
 - ✓ One-on-one or with multiple shareholders?
 - ✓ Proactively or reactively?
- What issues should be discussed?
- What executives should participate?
- What preparation do directors require?
- Do we need an engagement protocol to share with shareholders?



Accounting & Auditing Priorities

Accounting & Auditing Priorities



- FASB Priorities
 - ✓ Revenue Recognition

- SEC priorities
 - ✓ Shift from “neither admit, nor deny” settlement policy
 - ✓ Focus on quality of disclosures
 - ✓ Finish the implementation of Dodd-Frank regulations

- New COSO 2013 Framework
 - ✓ More evolutionary, than revolutionary
 - ✓ Supersedes old framework on December 15, 2014
 - ✓ Conduct a GAP analysis from current model to new 17 principles model

- Tax morality, transparency and base erosion and profit shifting (BEPS)

Accounting & Auditing Priorities (continued)



- PCAOB projects focused on the external auditor
 - ✓ Changes to Auditor's Reporting Model
 - ✓ Improving Audit Transparency
 - ✓ Auditing Standard on Related Parties
 - ✓ Staff Consultant Paper on Auditing Accounting Estimates & Fair Value Measurements
 - ✓ Staff Audit Practice Alert on Auditing Revenue



Appendix

Audit Committee Priorities for 2014

Audit Committee Responsibilities

- Stay focused on job #1: Financial accounting & reporting
- Monitor key PCAOB proposals potentially impacting the external auditor's role
- Leverage internal audit as a barometer of the company's financial health—helping the audit committee understand the quality of financial controls, processes, and people
- Make sure the company's ethics and compliance programs are keeping up with new vulnerabilities to fraud and misconduct
- Understand the company's tax risks and tax risk appetite; pay particular attention to the global “tax morality” and “tax transparency” debates, and assess the impact of tax on the company's brand

Audit Committee Priorities for 2014

Supporting the Board on Broader Governance Matters

- Understand how technology is continuing to transform the competitive landscape—and assess whether the board’s oversight processes enable directors to help lead the company forward
- Recognize that good risk management entails both defense and offense
- Set the tone and closely monitor leadership’s commitment to that tone, and actively “listen to the conversation” below senior management and outside the corporate office



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Recent Corporate Governance changes in the UK

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Topics

Audit Transparency

- Audit Committees' and Auditors' Reports

2014 UK Corporate Governance Code

- Risk Management and Internal Control
- Directors Remuneration
- Shareholder Engagement

Audit Committee Reports

- 'Audit committee reports' to include *inter alia*:
 - ✓ The significant issues considered by the audit committee in relation to the financial statements and how addressed
 - ✓ How the audit committee assessed the effectiveness of the audit process
- FRC Financial Reporting Lab
 - ✓ Context
 - ✓ What the committee did
 - ✓ What the committee concluded
 - ✓ Why the committee concluded what it did
 - ✓ Cross-references
 - ✓ Active language
- Disclosure shaping behaviour
- Disclosure colouring the readers impression (engaged and active, vs receiving and reviewing)

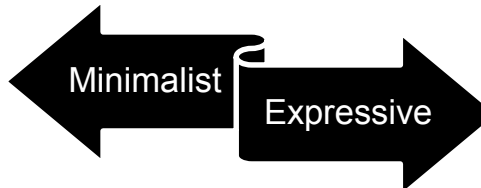


Audit Committees' and Auditors' reports – experience to date

Significant issues considered by the audit committee

Goodwill and intangible asset impairment reviews.

A paper outlining the key facts and judgements, prepared by management, was circulated to the Committee prior to the meeting at which it was discussed. Members of management attended the section of the meeting of the Committee where their paper was discussed to answer any questions or challenges posed by the Committee. The issues were also discussed with the external auditor. The Committee was satisfied that the significant issues have been appropriately addressed by management.



Goodwill and intangible asset impairment reviews.

Judgements largely related to the assumptions underlying the calculations used to value the businesses being tested. These assumptions included long-term business and macro-economic projections.

The Committee requested a number of clarifications to the internal guidance and reviewed detailed reports from management including the methodology applied to ensure the discount rates used are within an acceptable range. In addition, the Committee constructively challenged underlying assumptions used within short and long-term growth projections, including consideration of different scenarios. The Committee also considers detailed reporting from, and holds discussions with, the external Auditors. Following consideration of these reports, the Committee reviewed and agreed the impairment of £1.2 billion in Spain. Further detail on impairment can be found in note 11 on page 105. The Committee concluded that the intangible assets of our US business were not impaired and approved disclosures in our financial statements.

Audit Reports – Out with the old and in with the new

Binary

Generic explanation of an audit

Comparatively short

<p>Auditor's Reports on the Financial Statements and on Internal Control over Financial Reporting (Sarbanes-Oxley Act Section 404)</p> <p>The report set out below is provided in compliance with International Standards on Auditing (ISA) and Internal KPMG Audit PCA has also issued reports in accordance with standards of the Public Company Accounting Oversight Board in the US, which will be included in the Annual Report on Form 20-F to be filed with the US Securities and Exchange Commission. These reports are unaudited and include opinions on the Group Financial Statements and on the effectiveness of internal control over financial reporting as at 31 December 2012.</p> <p>Independent Auditor's Report to the Members of AstraZeneca PLC</p> <p>We have audited the Group Financial Statements of AstraZeneca PLC for the year ended 31 December 2012 set out on pages 142 to 151. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRS) as adopted by the EU.</p> <p>This report is made solely to the Company's members, as a whole, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and in respect of the separate opinion in relation to IFRS as issued by the International Accounting Standards Board (IASB), as amended that has been agreed with the Company. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state in our report as auditors in relation to the separate opinion in relation to IFRS as issued by the IASB, those matters that we have agreed to state in our report, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members, as a body, for our audit work, for this report, or for the opinions we have formed.</p> <p>Respective responsibilities of Directors and auditor</p> <p>The responsibilities of the Directors of the Company in relation to the preparation of the Financial Statements and Internal Control over Financial Reporting are set out on page 140. The Directors are responsible for the preparation of the Group Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the Group Financial Statements in accordance with applicable law and International Standards on Auditing (ISA) and Internal KPMG Audit PCA has also issued reports in accordance with standards of the Public Company Accounting Oversight Board in the US, which will be included in the Annual Report on Form 20-F to be filed with the US Securities and Exchange Commission. These reports are unaudited and include opinions on the Group Financial Statements and on the effectiveness of internal control over financial reporting as at 31 December 2012.</p> <p>Scope of the audit of the Financial Statements</p> <p>A description of the scope of an audit of financial statements is provided on the Financial Reporting Council website at: www.frc.org.uk/default.asp?menu=audit</p> <p>Opinion on Financial Statements</p> <p>In our opinion the Group Financial Statements:</p> <ul style="list-style-type: none"> give a true and fair view of the state of the Group's affairs as at 31 December 2012 and of its profit for the year then ended; have been properly prepared in accordance with IFRS as adopted by the EU; and have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the EU Regulations. <p>Other matters</p> <p>We have reported separately on the Parent Company Financial Statements of AstraZeneca PLC for the year ended 31 December 2012 and on the information in the Directors' Remuneration Report that is described as having been audited.</p> <p>James Daley Senior Statutory Auditor For and on behalf of KPMG Audit PCA, Statutory Auditor Chartered Accountants 15 Canale Street, London, E14 6UG, 20 January 2013</p>	<p>Company's Responsibilities</p> <p>The Directors' responsibility for the preparation of the Financial Statements and Internal Control over Financial Reporting is set out on page 140. 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These reports are unaudited and include opinions on the Group Financial Statements and on the effectiveness of internal control over financial reporting as at 31 December 2012.</p>	<p>Opinion on other matter prescribed by the Companies Act 2006</p> <p>In our opinion the information given in the Directors' Report for the financial year for which the Group Financial Statements are prepared is consistent with the Group Financial Statements.</p>	<p>Matters on which we are required to report by exception</p> <p>We have nothing to report in respect of the following:</p> <ul style="list-style-type: none"> Under the Companies Act 2006 we are required to report to you if, in our opinion: certain disclosures of Directors' Remuneration specified by law are not made; or we have not received all the information and explanations we require for our audit. <p>Under the Listing Rules we are required to review:</p> <ul style="list-style-type: none"> the Directors' Statement, set out on page 146, in relation to going concern; in Part of the Corporate Governance Statement on pages 110 to 117 relating to the Company's compliance with the provisions of the UK Corporate Governance Code specified for our review; and certain elements of the report to shareholders by the Board on Directors' Remuneration. 	<p>Other matters</p> <p>We have reported separately on the Parent Company Financial Statements of AstraZeneca PLC for the year ended 31 December 2012 and on the information in the Directors' Remuneration Report that is described as having been audited.</p>	<p>James Daley Senior Statutory Auditor For and on behalf of KPMG Audit PCA, Statutory Auditor Chartered Accountants 15 Canale Street, London, E14 6UG, 20 January 2013</p>	<p>Other matters</p> <p>We have reported separately on the Parent Company Financial Statements of AstraZeneca PLC for the year ended 31 December 2012 and on the information in the Directors' Remuneration Report that is described as having been audited.</p>	<p>James Daley Senior Statutory Auditor For and on behalf of KPMG Audit PCA, Statutory Auditor Chartered Accountants 15 Canale Street, London, E14 6UG, 20 January 2013</p>
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Specific description of the particular audit:

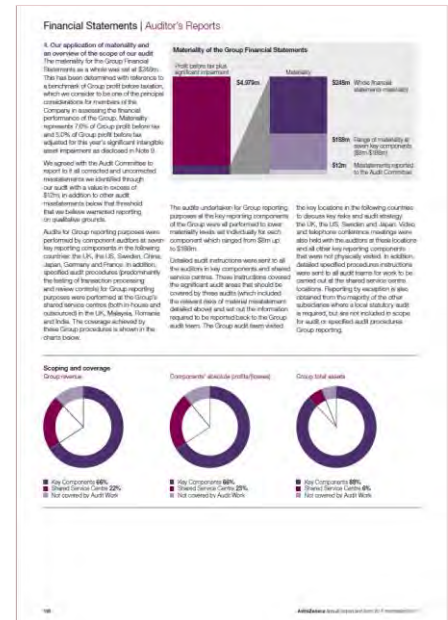
Audit risk (and how the auditor addressed them)

Audit materiality

Audit scope

Graphics

Comparatively long



Audit reports - What next?

- Auditing Standards require disclosure of 'audit risk'
- Best practice has led to disclosure of the 'auditor's response'
- ... but what about the 'audit findings'
 - ✓ How acceptable are the accounting policies?
 - ✓ How acceptable are the judgements and estimates?
 - ✓ How acceptable are the disclosures?



KPMG LLP (UK)
Audit

Audit reports – field testing a bold idea

Restoring Trust

Shaping the future of corporate reporting



Tony Cates

When I launched KPMG's Restoring Trust initiative last year I said that it was time for change. Since then we've seen immense change in audit reporting: the new "long form" audit report. I really do think it is a positive change, one that should help the dialogue between companies and shareholders. We haven't yet seen a complete season of these new reports, but, as I said in January when we published our survey of early reports, there are some great examples of what can be achieved. In a very short time we have come a very long way from the traditional binary audit opinion.

But what next?

The challenge is this. As it stands, a new audit report tells shareholders the key risks and the auditor's response to them – what the auditor did to address them. In other words, what risks did the auditor check under and how did he go about turning them over? However, it is not telling shareholders what the auditor found when he looked under those rocks. It does not say, for example, how acceptable the policies, estimates or disclosures were.

So we asked ourselves a simple question. Why not?

If we truly want audit to make a difference, not only do we have to ask these challenging questions, but offer bold answers – daring to think differently. So we have put it to the test by issuing a small number of audit reports that extend the new audit report, beyond the minimum required, by also setting out what we found. With the agreement of our clients, Rolls-Royce Holdings plc and New World Resources Plc – and we are very grateful to them for their commitment to shaping the future – the audit reports to their shareholders that do just that (some extracts are set out here). So whilst our KPMG reports normally set out under each audit issue, "the risk" and "our response", on these occasions we have added, "our findings".

“Our findings: We found that the Group has developed a framework for selecting the accounting basis to be used which is consistent with accounting standards and has applied this consistently. For almost all the agreements entered into during this year, it was clear which accounting basis should apply. Where there was room for interpretation, we found the Group's judgement to have been balanced.”

(report to Rolls-Royce Holdings plc shareholders)

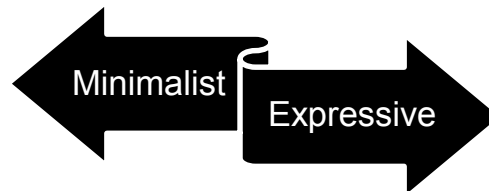
Audit Reports / March 2014

Audit reports – experience to date

Audit report (extracts)

Revenue recognition

We carried out testing relating to controls over revenue recognition, including the timing of revenue recognition, the recognition of revenue on a gross or net basis, the treatment of discounts, incentives and commissions and the accounting for multiple element arrangements, as well as substantive testing, analytical procedures and assessing whether the revenue recognition policies adopted complied with IFRS.



The basis of accounting for revenue and profit in the Civil aerospace business

Refer to page 81 (Key areas of judgement – Long-term aftermarket contracts), page 83 (Significant accounting policies – Revenue recognition) and page 44 (Audit committee report – Financial reporting)

The risk The amount of revenue and profit recognised in a year on the sale of engines and aftermarket services is dependent, inter alia, on the appropriate assessment of whether or not each long-term aftermarket contract for services is linked to or separate from the contract for sale of the related engines. As the commercial arrangements can be complex, significant judgement is applied in selecting the accounting basis in each case. The most significant risk is that the Group might inappropriately account for sales of engines and long term service agreements as a single arrangement for accounting purposes as this would usually lead to revenue and profit being recognised too early because the margin in the long term service agreement is usually higher than the margin in the engine sale agreement.

Our response We made our own independent assessment, with reference to the relevant accounting standards, of the accounting basis that should be applied to each long-term aftermarket contract entered into during the year and compared this to the accounting basis applied by the Group.

Our findings We found that the Group has developed a framework for selecting the accounting basis to be used which is consistent with accounting standards and has applied this consistently. For almost all the agreements entered into during this year, it was clear which accounting basis should apply. Where there was room for interpretation, we found the Group's judgement to have been balanced.

Agenda

Audit Transparency

- Audit Committees' and Auditors' Reports

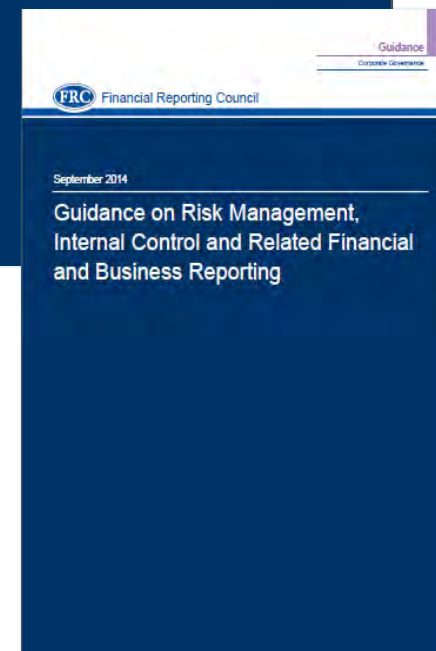
2014 UK Corporate Governance Code

- Risk Management and Internal Control
- Directors Remuneration
- Shareholder Engagement

UK Corporate Governance Code

Highlights

- Key revisions covering:
 - ✓ Risk management and internal control
 - ✓ Directors' remuneration
 - ✓ Shareholder engagement
- New Guidance on *Risk Management, Internal Control and Related Financial and Business Reporting* (what was the 'Turnbull Guidance')
- Applicable for periods beginning on or after 1 October 2014



UK Corporate Governance Code

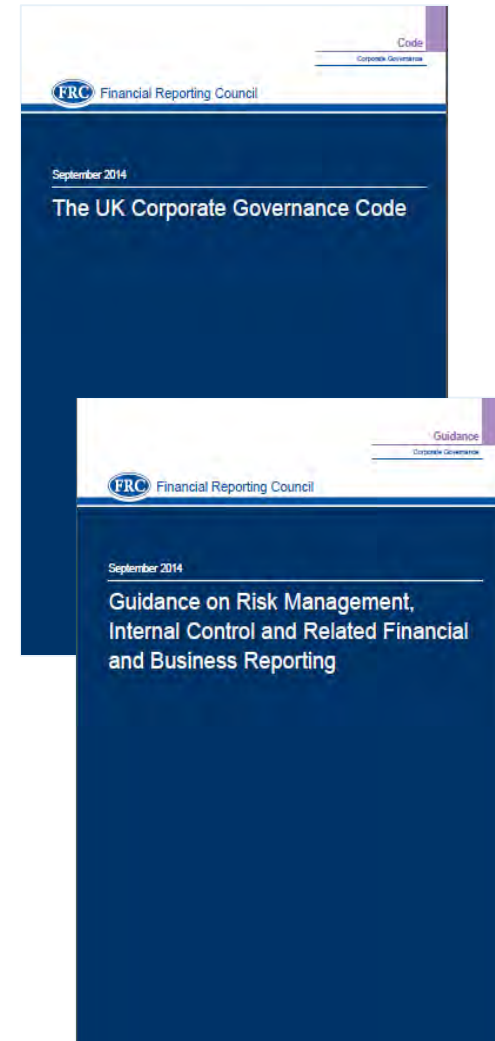
Risk management and internal control

- Expectation that the board monitors and reviews risk management and internal control systems on an ongoing basis

C.2.3 ... The board should monitor the company's risk management and internal control systems and, at least annually, carry out a review of their effectiveness, and report on that review in the annual report. The monitoring and review should cover all material controls, including financial, operational and compliance controls.

Paragraph 40 ... Regular reports to the board should provide a balanced assessment of the risks and the effectiveness of the systems of risk management and internal control in managing those risks. The board should form its own view on effectiveness, based on the evidence it obtains, exercising the standard of care generally applicable to directors in the exercise of their duties.

- Intended to convey that the board's involvement in risk and control systems should not be constrained to a one-off year end exercise



UK Corporate Governance Code

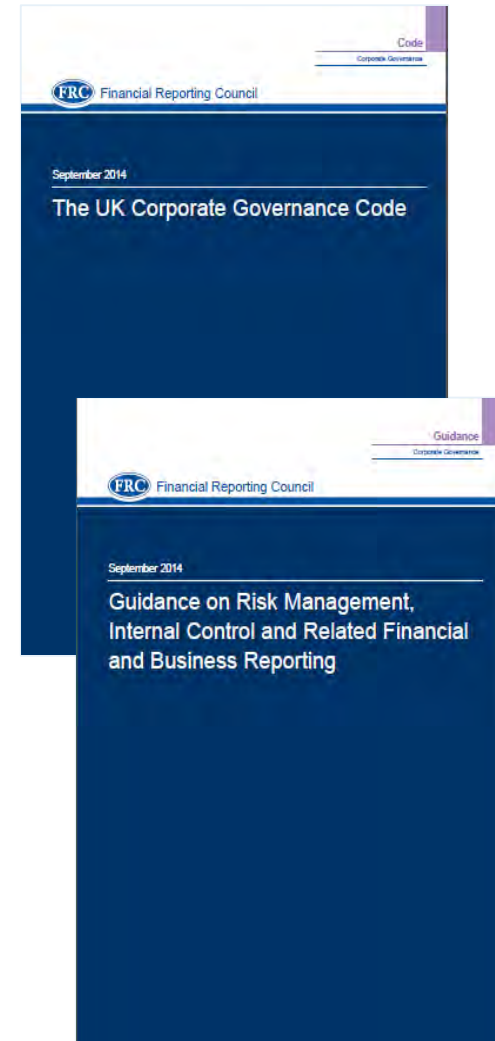
Risk management and internal control (continued)

- Explicit disclosure of the principal risks and how they are being mitigated

C.2.1 ... The directors should confirm in the annual report that they have carried out a robust assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity. The directors should describe those risks and explain how they are being managed or mitigated.

- A new long term viability statement

C.2.2. Taking account of the company's current position and principal risks, the directors should explain in the annual report how they have assessed the prospects of the company, over what period they have done so and why they consider that period to be appropriate. The directors should state whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, drawing attention to any qualifications or assumptions as necessary.



UK Corporate Governance Code

Directors' remuneration

- A 'comply or explain' presumption for clawback arrangements

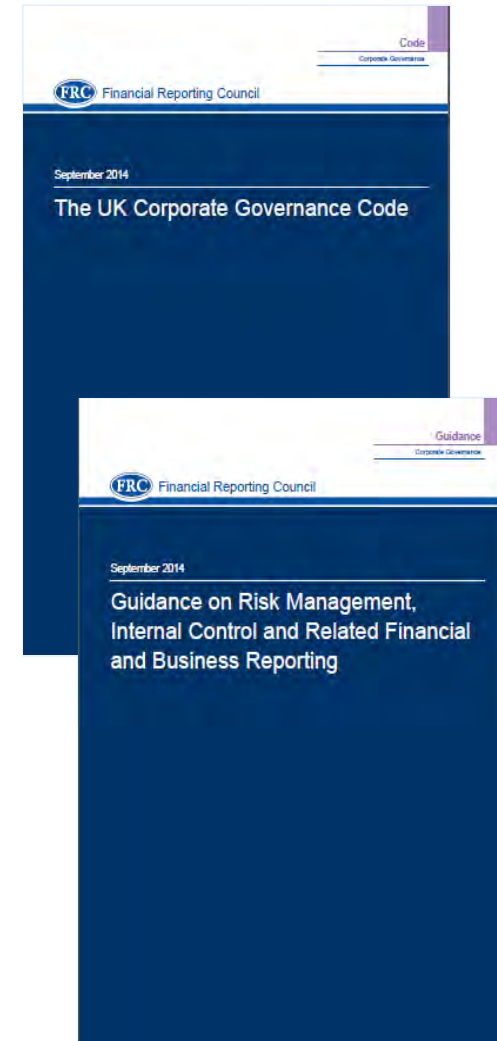
D.1.1 ... Schemes should include provisions that would enable the company to recover sums paid or withhold the payment of any sum, and specify the circumstances in which the committee considers it would be appropriate to do so

- Could impact as many as 90% of FTSE 250 companies

Shareholder engagement

- An explanation of how shareholder engagement will take place in the event of significant votes against a resolution – not the response to any concerns

E.2.2 ... When, in the opinion of the board, a significant proportion of votes have been cast against a resolution at any general meeting, the company should explain when announcing the results of voting what actions it intends to take to understand the reasons behind the vote result.



UK Corporate Governance Code

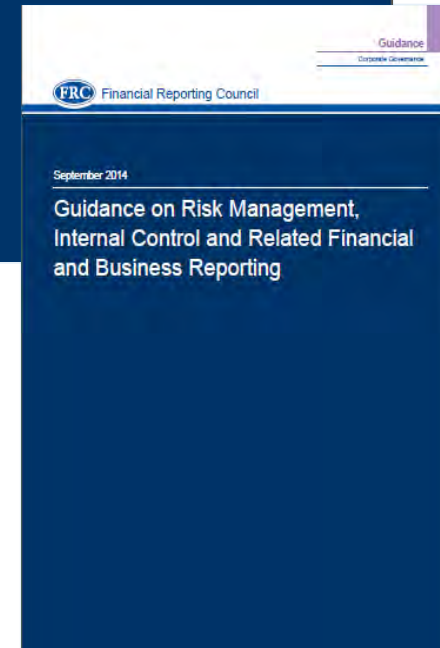
Guidance on Risk Management, Internal Control and Related Financial and Business Reporting

- Disclosure of 'uncrystallised' control failings

Paragraph 58 ... The board should explain what actions have been or are being taken to remedy any significant failings or weaknesses.

- ... but with a get out of jail free card?

Paragraph 58 ... *In reporting on these actions, the board would not be expected to disclose information which, in its opinion, would be prejudicial to its interests.*





cutting through complexity

EU Audit Reforms as adopted by the European Parliament and Council

Bermuda ACI Roundtable

October 27 & 28 2014



EU Audit Reform

1. Overview

2. Key elements of the legislation

- Scope – Public Interest Entity (PIE) definition
- Mandatory Firm Rotation (MFR)
- Non-Audit Services (NAS)
- Extra-territorial effect
- Audit report, regulators and the role of the Audit Committee

3. The next stage – Member State options and interpretation

4. What does this mean in practice?





1. Overview

Overview

- On 3 April 2014 the European Parliament voted to approve a Regulation and a Directive intended to reform the audit market in the EU.
- The Council of Ministers adopted the measures on 14 April 2014 thereby paving the way for the legislation to enter into force in the EU in June 2014.
- There is a two year transition period which means that the legislation is expected to become applicable in the 28 Member States of the European Union in June 2016.

The KPMG view

- The changes that this new legislation will bring about are significant. KPMG's view has always been that any measures should have a clear and unequivocal benefit to audit quality, provide for a robust framework for auditor independence and strengthen corporate governance.
- We believe the adoption of International Standards on Auditing, expanded auditor reporting requirements and the strengthening of the role of independent audit committees will positively contribute towards audit quality; in this regard we are supportive of the changes.
- We continue to believe, however, that other aspects of the legislation, such as mandatory firm rotation combined with significant restrictions on non-audit services, will inevitably reduce choice for shareholders, while increasing costs and complexity.



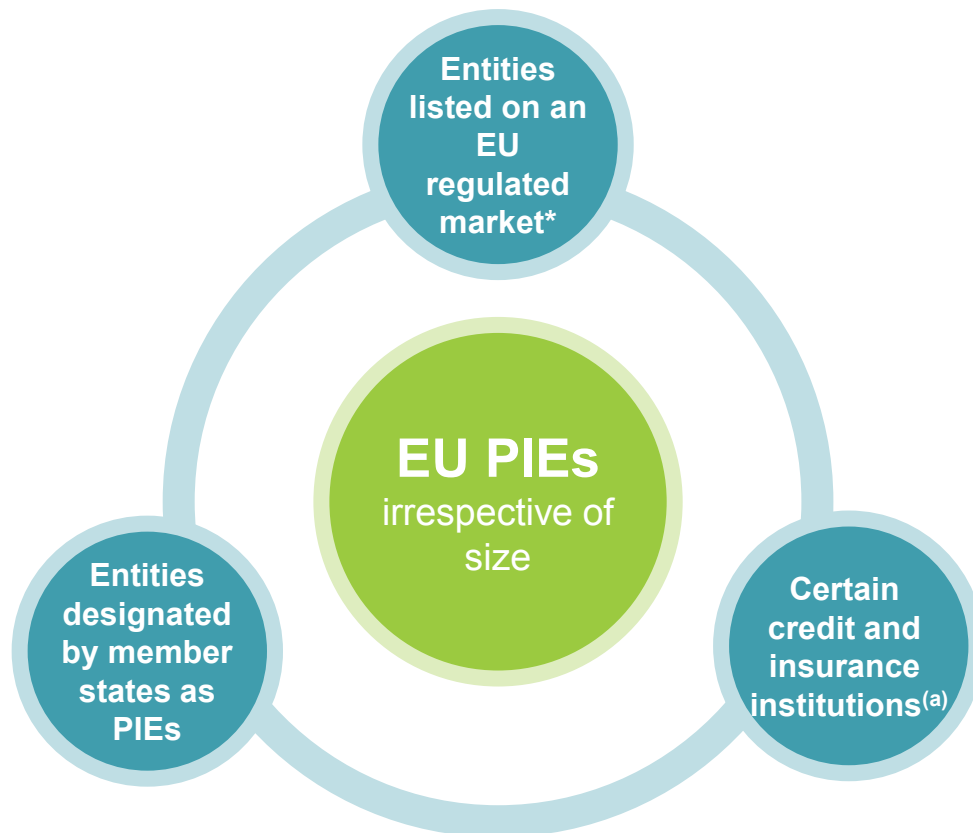
2. Key elements of the legislation



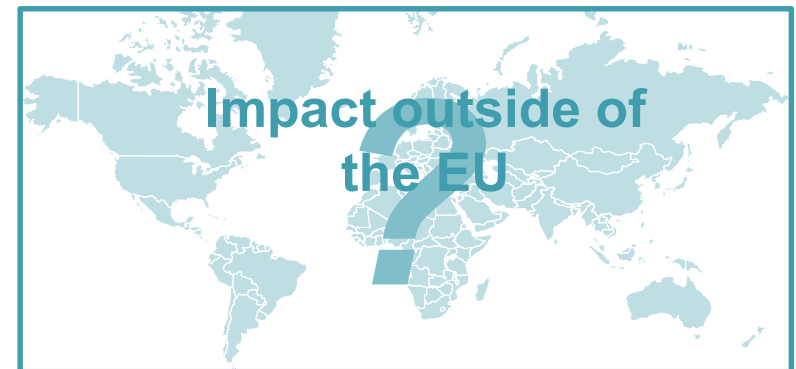
Public Interest Entities (PIEs)

Public Interest Entities (PIEs)

Which entities are affected by the regulation?



Note: (a) Including non-EU headquartered.



Impact outside of the EU:

The regulation will impact all entities governed by the law of a Member State that have listed securities in the EU; this would include the PIE subsidiaries of non-EU Groups.

*- <http://mifidatabase.esma.europa.eu>



Mandatory Firm Rotation (MFR)

Mandatory firm rotation (MFR)

MFR is required for all PIEs

- MFR required after a maximum duration of 10 years – though Member States may opt for a shorter maximum duration period. For example: Italy and the Netherlands will be able to retain their existing rotation requirements of nine years and eight years respectively;
- Member States have the option to allow PIEs to extend the maximum duration by:
- A further 10 years where a public tendering process is conducted for the statutory audit – to a maximum of 20 years; or
- A further 14 years where there is a joint audit arrangement – to a maximum of 24 years.

Transition measures for MFR (Regulation: Article 41 – see Appendix 4 for extract)





Non-Audit Services (NAS)

Non-Audit Services (Article 5)

- The Regulation contains a list of services which the statutory auditor of a PIE and all members of the statutory auditor's network are prohibited from providing to the PIE itself or to that PIE's EU controlled undertakings or its EU parent undertaking.
- The NAS prohibitions include, inter alia, tax compliance, tax advice, corporate finance and valuation services.
- Member States also have the option to allow certain tax and valuation services on condition that they do not have a direct effect on the financial statements or, if they do, that the effect is immaterial.
- The prohibitions in the Regulation are far more extensive than the rules in place in many EU Member States today and go well beyond the international independence requirements in the IESBA Code, SEC or PCAOB.

Non-Audit Services (Article 5)

Prohibited services to PIE audit clients



Any remaining permissible NAS capped at 70% of average fees paid in the last three consecutive years for the statutory audit

Non-Audit Services (Article 5)

Prohibited Tax services to PIE audit clients

i

Preparation of tax forms

ii

Payroll tax

iii

Customs duties

iv

Identification of public subsidies and tax incentives unless support from the statutory auditor or the audit firm in respect of such services is required by law

v



Support regarding tax inspections by tax authorities unless support from the statutory auditor or the audit firm in respect of such inspections is required by law

vi

Calculation of direct and indirect tax and deferred tax

vii

Provision of tax advice

Key:  Prohibited in all circumstances.
 Member States have the option to allow-see Slide 13 for requirements.

Non-Audit Services (Article 5)

Member State Options to allow certain prohibited services

Member States may allow certain services^(a) on condition that:



No **direct or have immaterial effect** separately or in aggregate on the audited financial statements



Estimation of the effect is **comprehensively documented** and explained in **additional report to the audit committee**



Principles of independence are complied with

Likely Impact:

1. Materiality exemption will be open to interpretation.
2. A patchwork of rules is likely to remain across the EU.
3. Unless Member States take up this exemption – there will be severe restrictions on providing tax services to audited public interest entities.

Note: (a) These services are highlighted in amber on Slides 11 and 12.

Non-Audit Services (Article 5)

What is the impact of timing?

The prohibitions will result in the need for careful consideration of the best timing for the appointment of Auditors **and** possible providers of prohibited Non-Audit Services



It is not permitted for the statutory auditor of a PIE to provide NAS within the EU during:

- The period between beginning of the period audited and the issuing of the audit report; and
- The financial year immediately preceding in relation to services relating to “designing and implementing internal control...financial information technology systems.”

The NAS requirements and prohibitions will come into legal effect **2 years after the date of entry into force** – estimated as June -2016.



**Extra-territorial
effect**

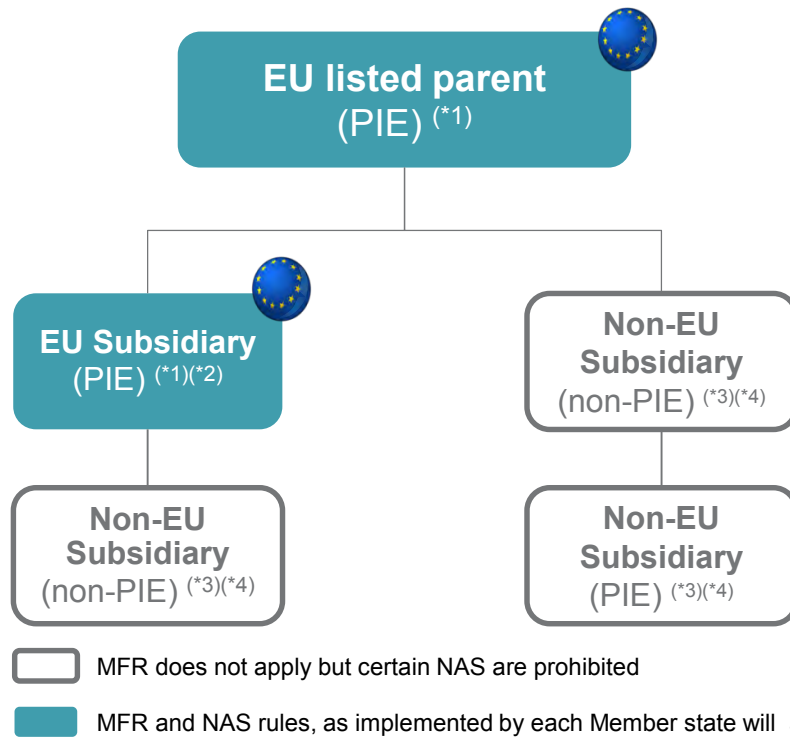
Extra-territorial effect

- Although the EU Regulation is primarily aimed at EU entities, the rules will also impact groups based outside the EU.
- The EU PIE definition will impact, for example, EU based subsidiaries of non-EU parent companies to the extent that those subsidiaries are either credit institutions, insurance undertakings or have debt or equity admitted to trading on an EU Regulated Market. To the extent that those entities meet the definition of an EU PIE they will be affected by the provisions set out in the Regulation – MFR, NAS etc.
- The following slide is an illustration of the impact on entities both inside and outside out of the EU in relation to MFR and NAS. Further examples are highlighted in the KPMG Frequently Asked Questions on the EU Audit Reform portal site at:

<https://portal.ema.kworld.kpmg.com/audit/EUAuditReforms/Pages/HomePage.aspx>

Who does it affect?

Within the EU and beyond



We can continue to provide services to non-EU subsidiaries provided that our independence as auditors of the PIE is not compromised by the provision of such services. However, some services are regarded as ALWAYS affecting that independence and so are always prohibited as follows:

- services that involve playing any part in the management or decision-making of the audited entity;
- bookkeeping and preparing accounting records and financial statements;
- designing and implementing internal control or risk management procedures related to the preparation and/or control of financial information or designing and implementing financial information technology systems.

Notes

- *1. The EU parent company auditor will rotate in line with the national law of the Member State where the parent is incorporated.
- *2. The rules apply such that any EU PIE subsidiaries are also subject to the NAS prohibitions. The EU PIE will also be subject to MFR as it is a PIE in its own right.
- *3. As the group contains an EU PIE, the rules in relation to the provision of NAS impact the statutory auditor and their member firm network. Network firms can continue to provide certain NAS services to the non-EU subsidiaries provided that the independence of the statutory auditors of the EU listed parent PIE is not compromised by the provision of such services. However, the text above specifies services that are always prohibited to the Network.
- *4. The entity is not an EU PIE (i.e.. not 'governed by' the law of an EU member state) therefore MFR does not apply.



Audit report, regulators and the role of the Audit Committee

Auditor reporting and regulators

AUDIT REPORTS and ISAs

- For PIEs: the audit report will include a description of the most significant assessed risks of material misstatement – including assessed risks of material misstatement due to fraud as well as a summary of the auditor's response to those risks
- The European Commission is empowered to adopt ISAs in Europe

REPORTS TO AUTHORITIES BY AUDITOR

Increased reporting by auditors to authorities including:

- Any material breach of the laws, regulations or administrative provisions
- Going concern – i.e. where there is 'a material threat or doubt concerning the continuous functioning of the public-interest entity'
- Modified audit opinions – i.e. 'a refusal to issue an audit opinion on the financial statements or the issuing of an adverse or qualified opinion'
- Suspected irregularities, including fraud, where the audited entity has not investigated

AUDITOR OVERSIGHT

- The CEAOB (Committee of European Audit Oversight Bodies) will take over the existing role of the EGAOB. It will be chaired by the Member States.
- The European Securities Markets Authority has a role as a non-voting observer on the CEAOB

OVERSIGHT FUNCTION

- Role of the audit profession: the PIE audits will be supervised by competent authorities that are independent of the profession. They may delegate tasks to other bodies. Non PIE inspections can continue to be performed by professional bodies

DIALOGUE BETWEEN REGULATORS AND AUDITORS

- Effective dialogue to be established between competent authorities supervising credit institutions and insurance and auditors of these entities. Guidelines will be provided.
- At least once a year the ESRB (European Systemic Risk Board) and the CEAOB shall organise a meeting with the auditors of all systemically important financial institutions in the EU

Impact on Audit Committees

ROLE OF THE AUDIT COMMITTEE

- Most of the requirements for audit committees as set out in the regulation represent current 'best practice'
- Clear encouragement to audit committees to consider smaller audit firms in a tender process
- All contractual clauses entered into between a PIE and a third party that restrict the choice to appoint a statutory auditor shall be 'null and void'

NON-AUDIT SERVICES

- Audit committee approval needed before allowing permissible non-audit services.
- Audit committees may also issue guidelines regarding the provision of tax and valuation services if a Member State exercises its option to permit these.
- Annually independence confirmation required by the statutory auditor in writing to the audit committee with an outline how any threats to independence were mitigated

MAKE-UP OF THE AUDIT COMMITTEE

- Independent non-executive members of either the administrative body or the supervisory body
- Members can be directly appointed at the Annual General Meeting
- At least one member of the audit committee must have competence in accounting and/or auditing. The members as a whole should have competence relevant to the sector in which the company has its business

REPORTING TO AUDIT COMMITTEES

- A written report providing detailed information on the results of the audit, with explanatory text (e.g. materiality level for classes of transactions).
- Report and explain judgments about events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern and whether they constitute a material uncertainty

The KPMG view

Auditing Standards and auditor reporting

- The adoption of International Standards on Auditing will help to promote greater consistency throughout the EU.
- We support expanded auditor reporting; the principles of the new report are substantially consistent with ongoing international developments such as those lead by the IAASB.

Enhancing the role of the audit committee

- We support strong, independent audit committees and believe that they should be actively involved in assessing audit quality and auditor independence, including approving any non-audit services to be provided by the auditor. We therefore support the measures taken to strengthen the role of the Audit Committee.
- Expanded reporting by the statutory auditor to the Audit Committee will promote greater transparency around the audit process, improving the awareness of audit committee members by increasing the focus on key audit issues.

The KPMG view

Strengthening of auditor oversight and communication with prudential regulators

- We welcome the creation of a new Committee of European Audit Oversight Bodies (the CEAOB) which we believe will contribute to promoting greater consistency in the EU.
- Increased three-way communication between auditors, banks and prudential regulators covering the major financial institutions should help to enhance the overall risk assessments made by the European Systemic Risk Board and promote greater transparency on broader systemic issues in the EU that may be identified from audits of SIFIs.

Known unknowns

Many areas still require clarification...

PIE definition

- Will Member States 'designate' additional PIEs ?

Clarity

- Many elements of the regulation still require clarification
- Member States (Governments, Professional Bodies etc.) are likely to issue consultations and guidance on the legislation
- The European Commission will play a central role in issuing interpretations and guidance to Member States

Country interpretation

- Will individual Member States implement the permitted derogations?
- Will Member States introduce additional restrictions?
- Risk of patchwork of rules across EU remains

Next stage:

The implementation of the legislation in each of the 28 EU Member States – interpretations, clarifications and selection of options will be critical.

Member State options

Flexibility in implementation

Likely patchwork of different requirements across the EU as each Member State considers available options

Prohibited Non-Audit Services (NAS)

- ▶ Add to the list of prohibited NAS
- ▶ Allow certain tax and valuation services to be provided by the auditor, subject to requirements of materiality, independence and disclosure

Public interest entities (PIEs)

- ▶ Expand the PIE definition to include any other entity e.g. by size, nature of business etc.

Terms of engagement and MFR

- ▶ Set a maximum duration (before MFR required) of less than ten years
- ▶ Allow for the extension of total permitted tenure of up to a maximum of 20 years (tender) and/or 24 years (joint audit)
- ▶ Require PIEs to appoint two auditors

Member States have a number of options in the Regulation....



Transparency

- ▶ Require the publication of findings from audit quality inspections (aggregated)

Permitted Non-Audit Services (NAS)

- ▶ Adopt a stricter cap on NAS fees than 70%
- ▶ Establish stricter rules for conditions under which permitted NAS may be provided

Audit Report

- ▶ Set additional requirements as to the content of the audit report

Audit Committee Reporting

- ▶ Set additional requirements in relation to the content of the additional report to the Audit Committee
- ▶ Require that the additional report to the Audit Committee be provided to third parties

Member State implementation and interpretation will be a key area of focus over the next 2 years

The KPMG view

- In many areas the legislation will, increase complexity and cost for business, reduce choice and create inconsistencies between Europe and the rest of the world. Notably:

Mandatory Firm Rotation (MFR) combined with further restrictions on non-audit services (NAS)

- We believe that mandatory audit firm rotation will reduce choice in the market place by removing the incumbent auditor from the tender process; other firms will also be unable to tender due to the expanded restrictions on non-audit services.

A regulatory patchwork in the EU

- The Member State options in the new Regulation gives Member States a significant degree of flexibility in interpretation and implementation of the new rules. Unfortunately, this flexibility will result in a patchwork of different requirements across the EU. The patchwork will create an unnecessarily complex and costly regulatory compliance environment for companies and their auditors in the EU.

Inconsistency with existing internationally recognised standards

- The new EU independence rules effectively prohibit many NAS that are permitted under other internationally recognised frameworks such as the IESBA Code of Ethics and by the SEC and PCAOB. The inconsistency with rules outside of the EU will again increase the cost and complexity of doing business in Europe.

The KPMG view

Significant extra-territorial reach

- Although the EU Regulation is primarily aimed at EU entities, the rules will also impact groups based outside the EU. The EU PIE definition will impact, for example, EU based subsidiaries of non-EU parent companies to the extent that those subsidiaries are either credit institutions, insurance undertakings or have debt or equity admitted to trading on an EU Regulated Market. To the extent that those entities meet the definition of an EU PIE they will be affected by all of the above measures.

It now falls to each of the National Governments of the 28 EU Member States to adapt to and apply the new legislation – KPMG is committed to working in the public interest with regulators, governments and the business community to ensure that the new legislation is implemented as effectively as possible.



cutting through complexity

Financial reporting, regulatory and COSO

Bermuda ACI Roundtable

October 27 & 28 2014
















IFRS 9 – Why is This Important?




- **IFRS 9 will impact all entities, but especially banks, insurers and other financial companies.**
- **The impact will vary between industries and entities.**
- **Your stakeholders/investors will want to talk about the impact on your business.**


Overview of IFRS 9



Topic	IFRS 9	Impact	
		Financial sector 	Other corporates 
Recognition and derecognition	IAS 39 model		
Classification and measurement	New model		 
Expected credit losses (Impairment)	New model		 
Hedge accounting	Amended model		 

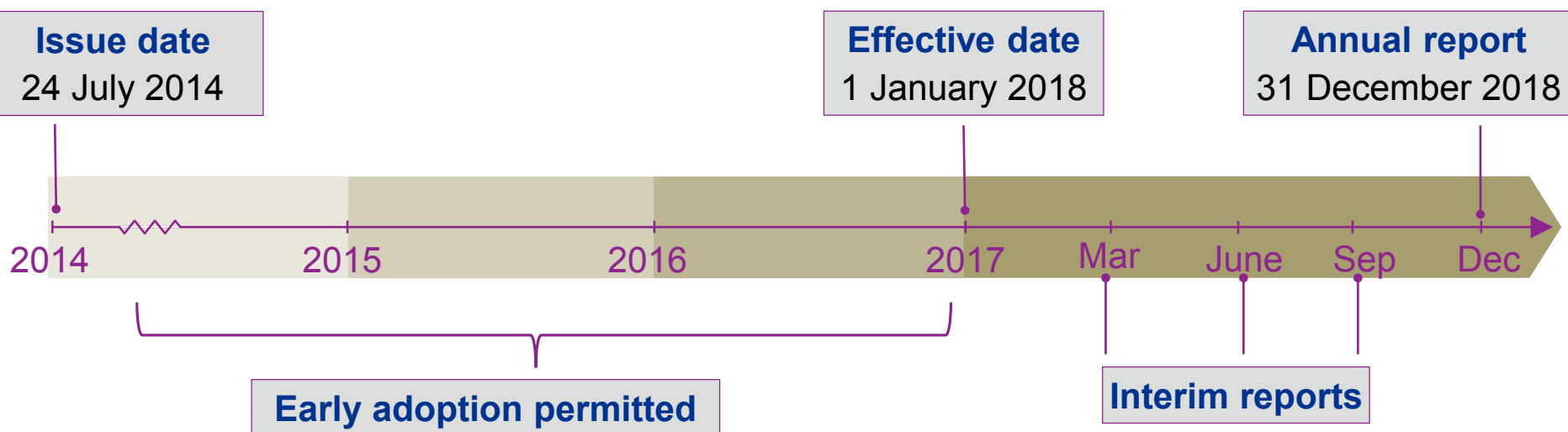
Legend:

 Low impact

 Medium impact

 High impact

Effective Date



- Entities that initially apply a previous version of IFRS 9 by 31 January 2015 can continue to apply that version until 1 January 2018.
- Permitted to early adopt 'own credit' requirements in isolation.

FASB Financial Instruments

Classification and measurement

- FASB decided NOT to continue to pursue cash flow characteristic assessment or the business model assessment
- Current U.S. GAAP would be retained for debt securities and loans
- Retains existing guidance for derivatives and bifurcation of embedded derivatives
- Equity securities would be measured at FV-NI unless certain exceptions are met
- Recently decided to keep FVO option as it currently exists in US GAAP (i.e. no specific conditions need to be met)
- Final standard expected Q4 2014

FASB Financial Instruments

Impairment

- Applicable to financial assets classified/measured at amortized cost and fair value with qualifying fair value changes recognized in other comprehensive income
- Move from incurred loss model to an expected loss model
- Debt securities retain existing guidance
- Differences to IFRS 9 exist:
 - FASB model: Allowance based on current estimate of contractual cash flows not expected to be collected based on:
 - Past events and current conditions,
 - Reasonable and supportable forecasts,
 - Unadjusted historical average loss experience (for periods beyond those reasonably and supportably forecasted)
 - IASB model: dual-measurement model including either lifetime expected losses or losses expected over next 12 months

IFRS 15 – Why is This Important?



- Revenue is a key metric for many entities.
- IFRS 15 introduces a new framework for the analysis of revenue transactions.
- The impact will vary between entities.
- Your stakeholders/investors will want to understand the impact on your business.

The Five Step Model Overview



1

Identify the contract with a customer

2

Identify the performance obligations

3

Determine the transaction price

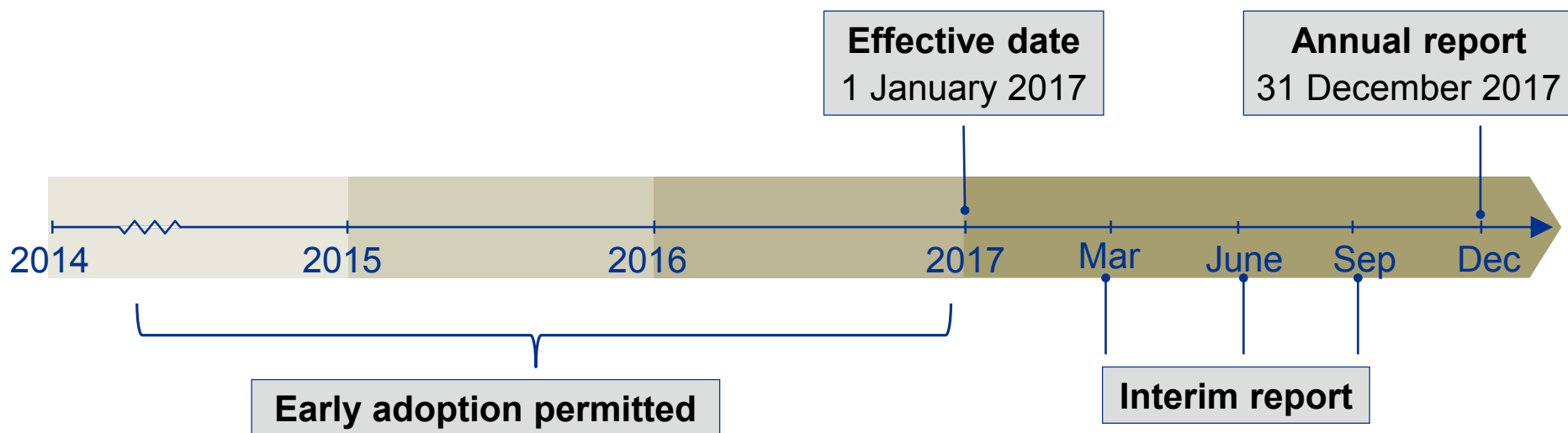
4

Allocate the transaction price

5

Recognize revenue

Key Facts – Effective Date



Impact sheet – Leases

Identifying all lease agreements and extracting lease data

- All leases longer than 12 months, including all renewal options, would be recognised on-balance sheet.
- It may require substantial effort to identify all lease agreements and extract all relevant lease data.
- To apply the simplified model for short-term leases, a company would need to identify the lease and key lease terms.

Changes in key financial metrics

- Key financial metrics would be affected by:
 - the recognition of new assets and liabilities; and
 - differences in the timing and classification of lease income/expense.
- This could impact debt covenants, tax balances and a company's ability to pay dividends.

New estimates and judgements

- The proposals introduce new estimates and judgemental thresholds that would affect the identification, classification and measurement of lease transactions.
- Senior staff would need to be involved in these decisions – both at lease commencement and at reporting period ends as a result of the continuous reassessment requirements.

Balance sheet volatility

- The proposals would introduce volatility to assets and liabilities for lessees, and for lessors in Type A leases, due to the proposed requirements to reassess certain key estimates and judgements at each reporting date.
- This may impact a company's ability to accurately predict and forecast results.

Changes in contract terms and business practices

- In order to minimise the impact of the proposals, some companies may wish to:
 - reconsider certain contract terms and business practices – e.g. changes in the structuring or pricing of a transaction;
 - look at lease length and renewal options, to use the short-term lease exemption to reduce reported lease liabilities; and
 - reconsider decisions with respect to buying or selling assets vs entering into lease transactions, including sale and leaseback transactions.
- The proposals are therefore likely to affect departments beyond financial reporting – including treasury, tax, legal, procurement, real estate, budgeting, sales, internal audit and IT.
- This may lead companies to re-evaluate their current organisational structure and reassess the resources currently focused on lease accounting.

New systems and processes

- Systems changes may be required to capture the data necessary to comply with the new requirements, including creating an inventory of all leases on transition.
- Processes would need to be reconsidered, to ensure that management judgement is exercised at key stages in preparing financial information.
- The complexity, judgement and continuous reassessment requirements would require additional resources focused on monitoring lease activity throughout the life of leases.
- Additional cross-organisational training for employees would be required.

Communication with stakeholders will require careful consideration

- Investors and other stakeholders will want to understand the impact of the proposals on the business.
- Areas of interest may include the effect of the proposals on financial results, the costs of implementation and any proposed changes to business practices.
- However, given that the proposals will remain under consultation until September 2013, the timeliness, content and cost-effectiveness of any analysis will require careful consideration.

THE BOTTOM LINE

The impacts of these changes may be felt right across your organisation.

Your financial ratios may be affected, which could impact your share price.

You need to start looking at your lease contracts now – does your company have the information and processes needed to implement these proposals?

Insurance contracts – US GAAP

- Decided NOT to continue a comprehensive project on accounting for insurance contracts
- Current scope in guidance remains unchanged
- Limited to insurance entities as described in current guidance
- Additional disclosures for short-duration contracts
 - ✓ Effective for public entities - December 31 2015
- Targeted Improvements to the accounting for long duration contracts –
 - ✓ Unsure on effective date, likely to be revised standard in 2015
- Stay tuned...

Insurance contracts – IFRS

- Redeliberations are ongoing, there has been changes from re-exposure draft
- Participating contracts next on IASB agenda
- Redeliberations expected to be complete early 2015
- Final standard expected mid-2015

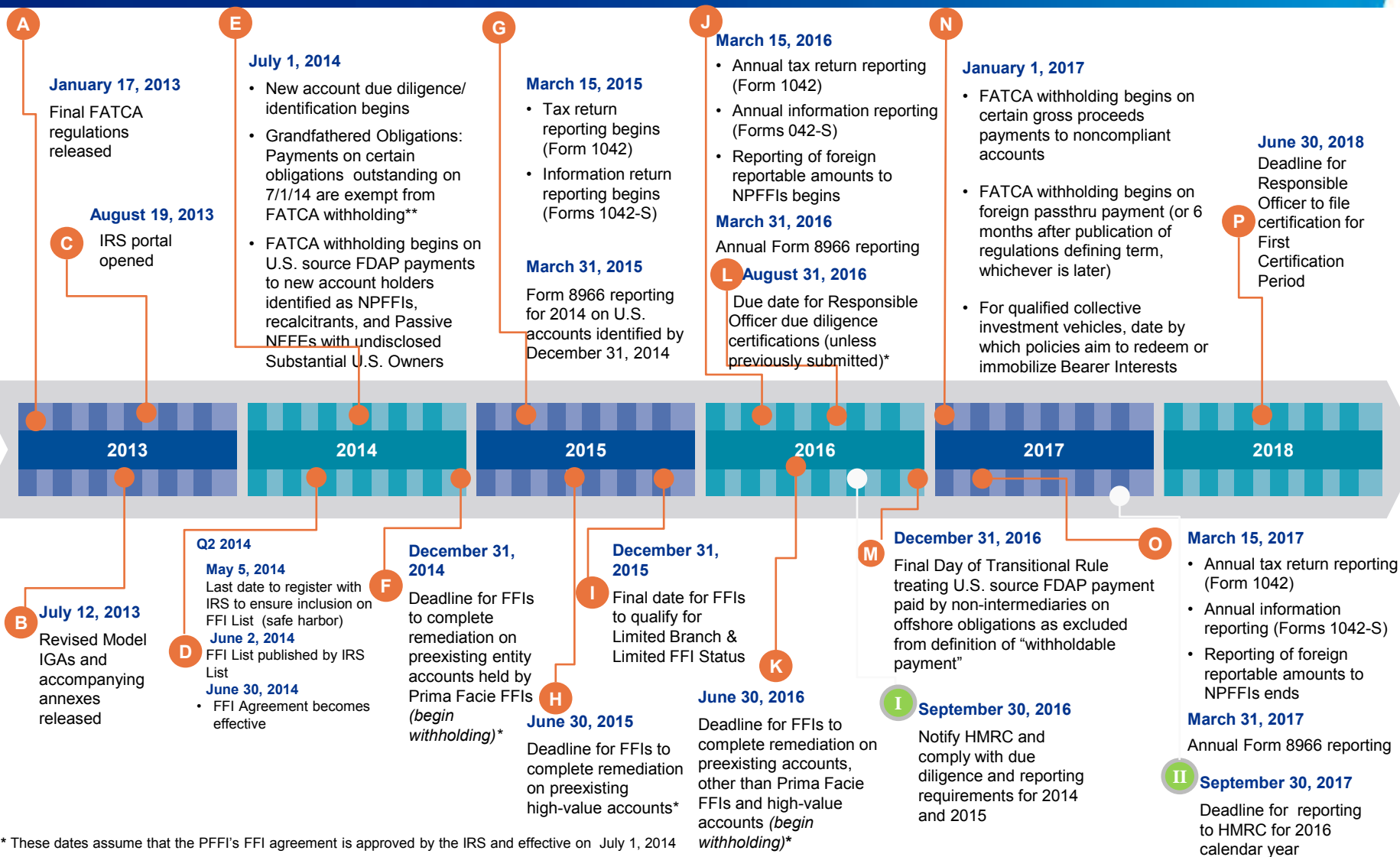


* The effective date of the final IFRS is expected to be approximately three years after the standard is issued. The IASB staff estimate that the issue date would be in 2015 – which would result in an expected effective date of annual reporting periods beginning on or after 1 January 2018, if the final standard is issued in early 2015. This appears to be the Board's target, given that the mandatory effective date of IFRS 9 is 1 January 2018.

Regulatory update – BMA and Solvency II

- Solvency II effective January 1, 2016
- EOIPA released draft guidelines in June 2014
 - ✓ Second set expected December 2014
 - ✓ Pillar 3 reporting next largest deliverable
- EOIPA visit in 2012 deemed BMA largely equivalent.
 - ✓ Largest caveat was Economic Balance Sheet (“EBS”) which is on BMA agenda
- How prepared are you for Solvency II and potentially EBS?
 - ✓ Focus to shift from understanding volume to speed of reporting
 - ✓ Financial reporting departments likely to be under strain

FATCA Time Line for Financial Institutions



* These dates assume that the PFFI's FFI agreement is approved by the IRS and effective on July 1, 2014

Workstreams clients must undertake if a financial institution for FATCA purposes

Entity classification



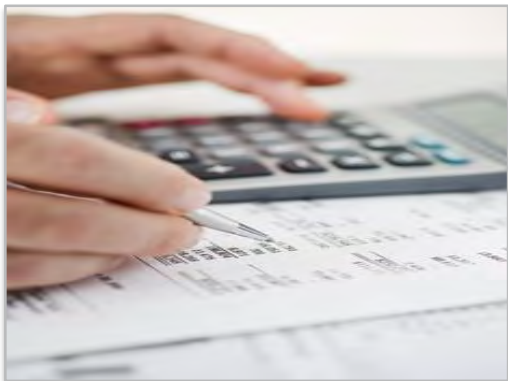
Client on-boarding



Back-book client identification and remediation



Withholding



Reporting



Governance/Compliance



Regulatory update – BMA other focus areas - AML

Amendments will be made to the following pieces of legislation that make up Bermuda's AML/ATF legal framework in order to bring Bermuda's AML/ATF legislation into compliance with the 2012 Revised FATF 40 Recommendation by the close of 2014:

- Proceeds of Crime Act 1997 ("POCA 1997")
- Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing) Regulations 2008 (the "Regulations"/"2008 Regulations")
- Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing Supervision and Enforcement) Act 2008 ("SEA 2008")
- Financial Intelligence Agency Act 2007 ("FIA 2007")
- Anti-Terrorism (Financial and Other Measures) Act 2004 ("ATFA 2004")
- Companies Act 1981 and Revenue Act 1898 ("RA") *(Due for an IMF visit in 2015)*

Source: www.namc.bm

EU AIFM Directive

The Alternative Investment Fund Managers Directive ('AIFMD') is an extra-territorial EU Directive that regulates the marketing of Alternative Investment Funds ("AIFs") to EU investors. The Directive came in to effect on 22 July 2013, with a transitional year being granted for managers to reach compliance. This transitional year expired on 21 July 2014.

Non-compliance with the Directive could result in regulatory sanction and investor recourse.

The marketing passport

- The AIFMD introduced a single "marketing passport" that enables AIFMs to market their fund products across all EU Member States. Whilst currently only available to EU AIFMs, legislation to enable non-EU AIFMs to obtain a marketing passport is expected in 2015. Applying for this passport will entail compliance with the full requirements of the AIFMD. AIFMs that have been lightly regulated in the past are likely to find AIFMD compliance to be a significant challenge.

•Private placement

- Non-EU AIFMs may currently only market fund products via the various national private placement regimes, the ease and usefulness of which vary significantly across the EU. In the UK, for example, the FCA requires only a simple notification before an AIFM can market. When considering whether or not to seek to raise capital within the EU, management may wish to factor a cost / benefit analysis into that decision, based on each jurisdiction's registration requirements.
- Registration for an NPPRs carries some additional compliance requirements, including additional disclosures to investors and regulatory reporting.

•Reverse solicitation

- This is where a prospective investor approaches a manager without any effort having been made by the manager in that regard — i.e. the manager has not undertaken any related marketing activity. This option at first appears attractive to managers as a means of continuing to access the EU market. In our experience, though, as managers explore this option the significant inherent risks of this strategy become apparent — essentially, inadvertently falling foul of marketing definitions, potentially leading to investor recourse and/or regulatory sanction, and the consequential reputational damage.

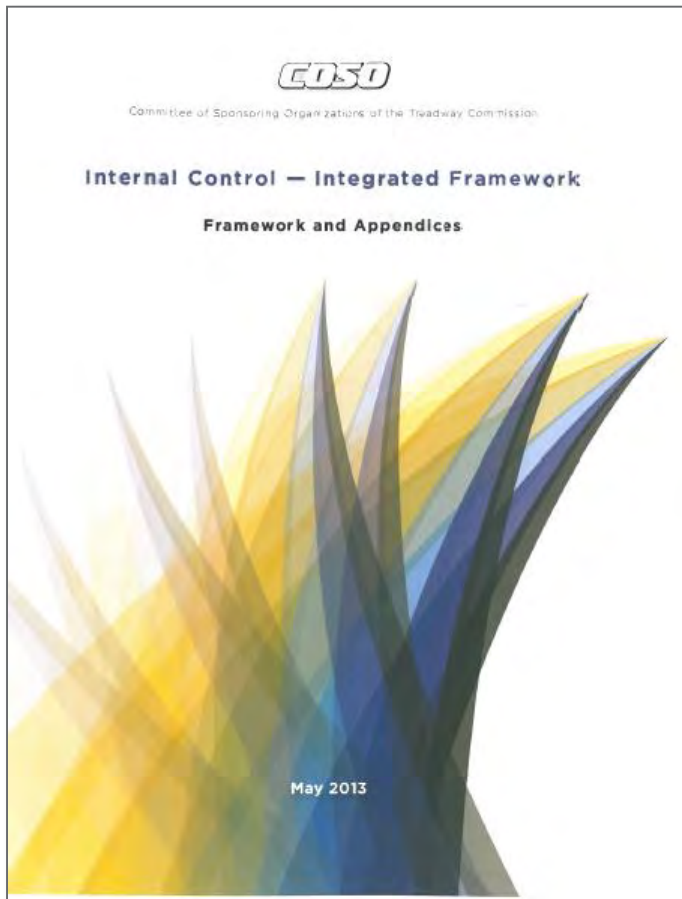
Regulatory update - PCAOB



- PCAOB projects focused on the external auditor
 - ✓ Changes to Auditor's Reporting Model
 - ✓ Improving Audit Transparency
 - ✓ Auditing Standard on Related Parties
 - ✓ Staff Consultant Paper on Auditing Accounting
 - ✓ Estimates & Fair Value Measurements
 - ✓ Staff Audit Practice Alert on Auditing Revenue

Transitioning to the COSO 2013 Framework: Considerations for the Audit Committee

Transitioning to the COSO 2013 Framework: Background



- Updated Internal Control – Integrated Framework (2013 Framework) issued on May 14, 2013
- Companion documents:
 - ✓ Internal Control – Integrated Framework: Executive Summary
 - ✓ Illustrative Tools for Assessing Effectiveness of a System of Internal Control
 - ✓ Internal Control Over External Financial Reporting: A Compendium of Approaches and Examples
- 2013 Framework will supersede 1992 Framework on December 15, 2014
- SEC plans to monitor transition phase, but has not issued transition guidance
- Role of audit committee in overseeing transition











2013 Framework: Articulates 17 Principles that Support the Five Components of Internal Control

To have an effective system of internal control:

- Each of the five components and 17 principles must be present and functioning
 - ✓ “Points of Focus” are provided to help understand each of the 17 principles
- The five components must operate together in an integrated manner

Control Environment	<ol style="list-style-type: none">1. Demonstrates commitment to integrity and ethical values2. Exercises oversight responsibility3. Establishes structure, authority and responsibility4. Demonstrates commitment to competence5. Enforces accountability
Risk Assessment	<ol style="list-style-type: none">6. Specifies suitable objectives7. Identifies and analyzes risks to objectives8. Assesses fraud risk9. Identifies and analyzes significant change
Control Activities	<ol style="list-style-type: none">10. Selects and develops control activities11. Selects and develops general controls over technology12. Deploys control activities through policies and procedures
Information & Communication	<ol style="list-style-type: none">13. Uses relevant, quality information14. Communicates internally15. Communicates externally
Monitoring Activities	<ol style="list-style-type: none">16. Conducts ongoing evaluations of effectiveness of internal controls17. Evaluates and communicates deficiencies

COSO 2013 Transition: Sample Project Plan

Activity	Deliverable	Who	Status	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB
Preliminary gap assessment and plan	Plan	John R.	Complete											
Complete mapping of controls to principles	ICOFR Memo (replaces Control Environment memo)	John R.	Complete											
Communicate gaps to control owners for action	Remediation Plans	Liz C.	Complete											
Remediation of any control and documentation gaps by identified control owners	Evidence of Remediation	Control Owners	In Progress											
COSO 2013 evaluation of the system of internal controls	Summary Evaluation Memo (Pro Forma and Final)	John R.	In Progress											
Monthly updates/reviews	Status vs Plan Issues & Remediation	John R. / Mike S.	In Progress											

 Audit Firm Check-in

Top 10 Areas That May Require Attention

- 1 Application of Principles and Points of Focus across the organization, at all levels
- 2 Evaluation of third party service organization arrangements
- 3 Board of Director oversight of internal control over financial reporting (Principle #2)
- 4 How incentives and rewards are aligned with fulfillment of internal control responsibilities (Principle #5)
- 5 Formal documentation of materiality assessments and risk tolerance (Principles #6 and #10)
- 6 Fraud Risk Assessment and determination of fraud risk controls (Principle #8)
- 7 The process for ensuring risk assessment and internal controls are responsive to change (Principle #9)
- 8 Linking general IT controls to related application controls (Principles #10 and #11)
- 9 Demonstrating that monitoring activities are built into business processes (Principle #12)
- 10 Demonstrating that the 17 principles and five components are present and functioning and that the components work in an integrated manner

...and the documentation of controls

Control Environment: Board Oversight



Principle #2 – The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control.

Points of focus to assist management in determining whether this Principle is present and functioning:

- The board identifies and accepts its oversight responsibilities in relation to the established requirements and expectations.
- The board defines, maintains, and periodically evaluates the skills and expertise needed among its members to enable them to ask probing questions of senior management and take commensurate actions.
- The board has sufficient members who are independent from management and objective in evaluations and decision-making.
- The board retains oversight responsibility for management's development and performance of internal control.

Transitioning to COSO 2013: Considerations for the Audit Committee



- Understand and monitor management's process and timeline for adopting the COSO 2013 Framework
 - ✓ How any gaps between the old and updated Frameworks are being identified
 - ✓ Impact of adoption of updated Framework
- Plan sufficient time for testing and remediation of deficiencies
- Be sure internal audit is involved, as appropriate
- Opportunity to take a fresh look!
- If company is not transitioning to updated Framework for 2014, disclosure plans
- If 2014 implementation is not well underway yet – *don't rush it*



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