

RESEARCH ARTICLE

Role Effectiveness of Audit Committees' Comparative Analysis between UK and Egypt

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Abstract

In recent years, academic attention on internal audit and corporate governance has grown very much, especially due to the collapse of many corporations around the world. Also, another motivation for this increase in studies is related to the evolving and expanding role of internal audit as a major corporate governance mechanism but also as an internal consultancy service. Thus, since during the last years corporate governance has received very much attention (due to its importance), not only from regulators but also from scholars, resulting in highlighting the significance of the internal audit, this research focuses on changes in the internal audit conditioned by the corporate governance. The main goal of this paper is to chart the similarities and differences, evolution and possible direction of audit committees across the two board structures widespread today within Europe. In this respect, an empirical study of audit committees across the UK, and Egypt will be performed. This is to encompass the unitary board perspective prevalent in the UK, the dual-board perspective prevalent in Egypt. To assess the similarities and differences of audit committees, a total of 6 companies and their annual reports were analysed. The companies reviewed were selected from high capitalisation indexes in the relative countries: The FTSE-100 for the UK and the EGX- 30 for Egypt.

Keywords: *Audit committees, Corporate governance, Egypt, Internal audit, UK.*

Introduction

Effectiveness is defined by the Oxford Online Dictionary as “the degree to which something is successful in producing a desired result”. In respect to an Audit Commission, the desired result is providing high quality financial reporting and consolidating investors' confidence in the financial reporting in order to provide good corporate governance. In the internal and external audit, the ASX CGC set various responsibilities and roles for the Australian Audit Commissions and all these responsibilities and roles can help valorise the effectiveness. Obviously, the concept of Audit Commission effectiveness has a dose of subjectivity and combined with the issue of data available for the public, make it difficult to empirical examine the notion of Audit Commission effectiveness.

Returning to the ASX CGC, its

recommendations from 2007 impose at least five requirements for effectiveness [1]. First of all, an independent chair, distinct from the chair of the board, chairs the Audit Commission. Second, all members are required financial studies, only some need to be acquainted with the industry of the firm and at least one member should have expertise and experience as a finance professional with proficiency in accounting and financial matters. Third, in order to operate properly, the Audit Commission requires at least three members. Fourth, even though the ASX CGC doesn't specify how many meetings the Audit Commission should have every year in order to carry out its duties effectively sufficient meetings (at least three a year) must be held. Fifth, a formal charter of the Commission is recommended.

Specialised literature also promoted different parameters for Audit Commission effectiveness. For instance, DeZoort and his collaborators [2] consider that an Audit Commission is effective when her members are qualified and possess the authority and the resources to act in the benefit of their stakeholders by properly carrying out their duties: internal controls, reliable financial reporting and risk management. Kalbers and Fogarty [3] also consider that in order for an Audit Commission to be effective, it must have the capacity to identify and execute certain responsibilities that might have been overlooked. However, Carcello and his collaborators [4] suggest that AC effectiveness is, in fact, the competence that allows it to oversee the internal audit function activities which are evaluated by total internal audit budget assigned to the internal audit function.

Another interesting definition is that of Goodwin and Yeo [5] who see in effectiveness the ability to hold over the independence of the internal audit function. Returning to Carcello, in 2002 he has characterised the effectiveness of an Audit Commission as the aptitude for protecting the interests of the shareholders by acquiring higher quality audit services, despite the higher fees. Similarly, Abbott et al. [6] argued that the Audit Commission effectiveness is an ability to preserve the independence of the external auditor which can be evaluated by the ratio of non-audit fees to audit services fees.

A brief literature review in respect to Audit Commission effectiveness highlights various features that reflect the effectiveness of an Audit Commission. The five characteristics analysed in this study are: the independence of Audit Commission chair, the financial and industry expertise of Audit Commission members, the frequency of meetings of Audit Commission, the dimensions of the Audit Commission and the formal charter of Audit Commission (ASX CGC's 2007 recommendations).

Features that Reflect Audit Commission Effectiveness

Independence of Audit Commission Chair

A very important characteristic that determines Audit Commission effectiveness is the independence of the members and chair. Fama and Jensen [7] suggested that independent members such as external directors may consider the directorate as a possibility for enhancing their reputations as experts in decision control. The ASX CGC [1] recommendations suggest the Audit Commission to be formed by non-executive directors, the majority of directors to be independent and also, the Audit Commission to be chaired by an independent chair distinct from the chair of the board. Previous studies which promoted the idea that AC independence impacts on the committee's effectiveness support all these recommendations [8].

Moreover, other studies also suggest that Audit Commission can raise the quality of financial reporting. For instance, Beasley and his collaborators [9] concluded that cases of illegal reporting firms are much rarer if companies have an Audit Commission that is dynamic and independent. Similarly, Abbott and Parker [10] argue that the Audit Commissions less likely to be sanctioned for illegal or misleading reporting are those formed of independent directors and have at least two meetings a year. Later in 2004, Abbott and his collaborators discovered that the independence is essentially and negatively influenced by the earnings management.

Additionally, Klein [11] and Carcello and Neal [12] who talk about Audit Commissions whose members are independent to be more effective in observing the corporate financial accounting operations. On the other hand, other scholars were unsuccessful in finding a link between independence and the occurrence of earnings restatements or quarterly earnings management [13] or discretionary accruals [14].

Frequency of Meetings of Audit Commission

Even though ASX CGC does not precisely indicate how many meetings an Audit Commission should hold each year because this number varies in relation to the size and the risk of the business, evidence shows that

these meetings are important [14] [8]. Beasley et al. [9] highlighting the fact that frequent Audit Commission meetings are associated with less fraud. Similarly, Xie et al. [14] concluded that these meetings also determine lower levels of discretionary current accruals. Accordingly, Abbott and his collaborators [8] discovered that those commissions that meet at least four times a year are less likely to reiterate their annual reports. Therefore, these studies show that Audit Commissions that meet frequently have more chances to be acquainted with the current auditing problems organizations face and are more careful in completing their duties.

Conversely, other studies found no evidence between the number of Audit Commission meetings and illegalities [8] or earnings management [13]. Neither, Davidson and his collaborators were able to find data in support to a relevant relation between the number of Audit Commission meetings and earnings management.

Size of Audit Commission

The size of the Audit Commission is another important characteristic in the evaluation of the Audit Commission effectiveness. According to the ASX CGC [1] Recommendation, the commission should have at least three members but it isn't specified a maximum number of members. Therefore, not setting an upper limit on the members' number it raises the issue whether larger commissions would translate into a more effective monitoring.

It is believed that a larger commission provides better quality financial reporting considering the fact that such an Audit Commission can easily identify and resolve issues in the financial reporting process [15]. Moreover, organizations with an Audit Commission with at least four members have lesser chances to have earnings restatements [16]. Additionally, Dalton et al. [17] discovered a positive relation between the Audit Commission's dimension and the supervising and monitoring function of the board. On the other hand, Xie et al. [14] emphasised the weak link existent between earnings management and the size of the commission and his perspective is also

supported by Abbott et al. [8]. Therefore, some studies suggest that larger number of members helps to achieve a better monitoring and also ASX CGC [1] recommends at least three members for an Audit Commission, leaving companies to decide if they want more than three members. This paper also promotes the idea that a larger Audit Commission is more likely achieve a better monitoring because it would have more diverse skills and perspectives.

Formal Charter of Audit Commission

A formal charter is essential for an Audit Commission because it offers the chance for clear distribution of rights, roles and responsibilities of the members and, at the same time, it provides a framework of procedures for the meetings. In respect to achieving effectiveness, the formal charter is one of the most important factors. Moreover, ASX CGC also recommends Audit Commissions to have a formal charter [1]. Despite this, rather few studies have discussed the issue of the charter. Rezaee and his collaborators [18] analysed this topic of the Audit Commission charters of Fortune 100 companies and discovered that over nine per cent of charters indicate the composition, independence, qualifications and financial expertise of their members. Also, a formal charter is an indicator for authoritative decision making [3].

Audit Commission Observing the Quality of the Internal Audit Function

Among the responsibilities of an Audit Commission is monitoring the internal audit function's procedures and policies. However, according to Goodwin and Yeo [5], the relation between internal audit function and the Audit Commission is, much more than that of overseen and overseer. In order to achieve and preserve good corporate governance, communication between the internal auditors and the Audit Commission is crucial [19, 20].

In their study, Gwilliam and Kilcommins [21] concluded that the Audit Commission enhances independence of internal audit function, at least on a perception level.

Others suggests that the Audit Commission's position is strengthened depending on the performance of the internal audit function. Because an Audit Commission does not have direct access to the same level of information as the management, an organization's internal audit function contributes to minimising issues related to agency theory and information [22]. In order to be most effective, Rezaee and Lander [23] highlight the importance of a year round working relationship between the internal audit function and the Audit Commission. Additionally, Zaman and Sarens [24] argue that Audit Commission and internal audit function establishing informal relations besides formal regular meetings offer more opportunities for Audit Commission to observe the internal audit function. In the following I will present and analyse literature on the topic of the relationship between the Audit Commission and the internal audit function.

Existent Studies

Scarborough and his collaborators analysed the link between the Audit Commission's structure and their relationship with the internal audit function. The researchers examined CIAs of Canadian largest manufacturing entities. Their findings showed that there are no relevant differences regarding the influence in resolutions to dismiss the CIA. Moreover, when Audit Commissions are formed only of external directors they will have more frequent meetings with the CIA and review the internal auditing schedule. Also, Raghunandan et al. [25] brought forward empirical data in support to the perceived level of information of Audit Commissions. The main results showed that Audit Commissions that offered private access to their CIA and revised both the plans and results of internal auditing have better chances to be acknowledged by their CIA. More recently, Raghunandan et al. [22] carried out another study and consistent with Scarborough et al.[19] they found that Audit Commissions formed only of independent directors and with at least one member having an accounting or finance background are more likely to have longer meetings with CIA, offer private access to

CIA and revise internal audit proposals and results of internal auditing.

Similarly, Goodwin [5] analysed the influence of financial expertise and independence on Audit Commissions relationship with the internal audit function. The study utilised data from Australia and New Zealand and focused on Audit Commissions and internal audit functions in both public and private sector. The study showed that accounting experience and independence have a complementary influence on Audit Commission relationship with the internal audit function. Apparently, independence is more linked to the process while accounting experience is linked to the measure of the reviews of the Audit Commission on the work of the internal audit function.

On the other hand, Carcello et al. [4] examined United States public investment companies in internal auditing. The surveys indicated a propensity for CIA of medium sized public entities combined with data available publicly. In the United States, Abbott and his collaborators [4] examined the link between the Audit Commission's supervising of the internal audit function and the nature of internal audit function operations by analysing top CIAs from Fortune 1000. They found a positive and strong connection between the commission's oversight variable and the budget assigned for internal-controls-based operations.

Furthermore, Cooper's [26, 27] qualitative study approached the issue of formation and membership of an Audit Commission and the relation between the Commission and internal audit in Australia. Cooper suggested that an effective and uniform relation between the Audit Commission and internal audit can have a positive effect on corporate management and control. Lastly, Abbott et al. [6] have analysed the connection between Audit Commission effectiveness and internal audit outsourcing and found that companies with effective Audit Commissions have fewer chances to outsource internal auditing to the external auditor. In addition, effective Audit Commissions that have authority over the CIAs' rejections will have an increasingly

negative relationship with the extent of outsourcing.

Comparative Assessment

Generally, previous works have found that an effective Audit Commission can raise the status of the internal audit function and at the same time, the internal audit function will impact positively the Audit Commission in its supervising role [6] [26].

In respect to the collaboration between the Audit Commission and the internal audit function, scholars like Scarbrough and his collaborators [35] [19] and Raghunandan and his collaborators [22] studied the relationship between the Audit Commission composition and the committee's collaboration with the internal auditing department. Scarbrough et al.'s [19] analysis is carried out in Canada, while Raghunandan et al.'s [22], paper is more recent and was performed in the United States. Both papers found that Audit Commissions formed only of external directors have more frequent meetings with the CIA and revise the internal auditing schedule. Consistently, Goodwin [28] performed a similar study in Australia and New Zealand where he differentiated the impact of accounting experience and independence on Audit Commission association with the internal audit function. The study showed that independence and financial expertise have a complementary impact on Audit Commission collaboration with internal audit.

However, regarding the perception and the observed level of expertise of Audit Commission, Raghunandan et al. [25] found that Audit Commissions that offered private access to their CIAs and revised the schedule and output of internal auditing have more chances to be acknowledged. Therefore, we can consider that Audit Commissions exercising their function as an internal control observer can have a solid and positive impact on corporate management. On the other hand, Abbott and his collaborators [26] used the supervising function of the Audit Commission as a direct measure in their analysis. They also have surveyed top entities from Fortune 1000. They observed that the commissions with an extended

supervising function are associated with a propensity for long hours allocated towards internal control activities. In other words, better internal controls may lead to higher internal audit function attention on internal controls.

Audit Commission Ensuring the Independence of the Internal Audit Function

The Institute of Internal Auditors (IIA) defines internal auditing as an objective, independent assurance and consulting operation designed to evaluate and improve a company's activity. According to the Institute of Internal Auditors, we can distinguish two very important features -the organisational independence of the internal audit function and the individual objectivity of internal auditors. The standard recommendations suggest CIA to report to a level within the organization in order to permit the internal audit function to carry out its responsibilities. Best practices indicate that the CIA should report directly to the Audit Commission or its equivalent in order to achieve necessary independence. In daily administrative activities, the CIA is recommended to report to the most senior executive [29].

The IIA stipulates that Audit Commissions and internal auditors have reciprocal objectives. Obviously, it is necessary to have a good and lucrative working relationship between the internal auditors and a company's Audit Commission. In order to achieve this objective, it is required an efficient channel of communication between the CIA and the Audit Commission and also it is necessary for the CIA to have access to the Audit Commission, to participate to the meetings of the Audit Commission, to advance the audit plan, to report on the output of major audits and essential audit results or other problems, and to debate internal auditing issues on risk and internal controls within the company [29]. Additionally, CIA and Audit Commission are required to meet regularly even without senior management and external auditors attending the meeting.

In the following I will analyse the existent works and researches that have examined

the relationship between Audit Commission and internal audit function independence.

Existent Studies

According to Goodwin and Yeo [28] the association between internal audit and Audit Commission may impact negatively the independence of the entity while transforming internal audit function in an exercise of management may impact individual objectivity. In a study promoted in Singapore, the authors discovered that an effective Audit Commission can help strengthening the status of the internal audit function by assuming the role of an independent and objective forum in which internal auditors may debate issues influencing the management. Furthermore, Christopher and his collaborators [30] examined the independence of the internal audit function through its collaboration with the management and the Audit Commission and based on survey of 34 CIAs from the Australian corporate sector, they found a number of risks for independence such as: the Audit Commission not having sole responsibility for appointing and dismissing the CIA, not reporting functionally to the Audit Commission, Audit Commission insufficient accounting expertise and having the CEO and CFO approve the internal audit budget and being involved in the audit plan.

In New Zealand, Van Peursem [31] examined the internal auditor's role and focused on the issue how an effective internal auditor can manage the difficulties of working with management to improve performance while also maintaining objectivity and independence from management in order to report on their activity and performance. Their findings showed that an internal auditor's close relationship with management can pose a risk for their independence in relation to management. In Akinteye et al. [32] explored the effects of managers' perceptions of internal and external auditing on the potential commission of financial reporting irregularities. They concluded that an independent internal audit function, in respect to reporting level, will determine an ameliorated control environment and a minimisation in reporting faulty results [33].

Similarly, Grambling et al. [34] support their results promoting the idea that independence through adequate reporting relationship is considered crucial.

Depending on who has the responsibility and authority for hiring and firing the CIA, independence of the internal audit function may also be negatively influenced. Accordingly, McHugh and Raghunandan [35] discovered that numerous internal auditors opinionated that investing the Audit Commission with hiring or firing authority would strengthen the independence of the internal audit function and enhance the ability of internal auditors to generate action on audit results. However, from a cognitive approach on internal auditor independence, Ahmad and Taylor [36] elaborated a framework for the notions of role conflict, role ambiguity and commitment to independence, in order to find proof of the effect of the role conflict and ambiguity, and their sub-dimensions, on the internal auditor's independence. In respect to role ambiguity and role conflict, the authors showed that those are considerable negatively associated to commitment to independence.

Comparative Evaluation

Having as a starting point the researches mentioned above, in the following I will focus on the consequences of Audit Commission granting the independence of the internal audit function. The majority of studies like: Christopher et al., [30]; Van Peursem [31]; McHugh and Raghunandan, [35] showed that the independence of the internal audit function is essential in a company [33]. The enlarged responsibilities of the internal audit function in the context of a dynamic business world, together with globalisation and increasing economic competition are pressuring the internal audit function which can put at risk its independence [37]. Other authors amongst who Christopher et al. [30], Van Peursem [31] and Goodwin and Yeo [28], support these views and investigated the independence of internal audit function in the context of the working relations with the management and Audit Commission. Even though these surveys are carried out in three different countries (New Zealand, Australia

and Singapore) each with its own particularities, the results were the same in all of the three studies. Goodwin and Yeo [28] and Christopher et al. [30] observed that an effective Audit Commission which is performing all its responsibilities can consolidate the independence position of the internal audit function.

Other scholars, Schneider and Wilner's [33] and Ahmad and Taylor's [36] examined the perception of independence of the internal auditor. Schneider and Wilner [33] investigated the implications of managers' perceptions of internal and external auditing on the potential of reporting irregularities of financial commission in the United States and, at the same time, Ahmad and Taylor [36] elaborated a framework for the notion of commitment to independence. Schneider and Wilner [33] highlight the importance of independence through proper reporting. A study conducted in Malaysia by Ahmad and Taylor's [36] showed that the greatest impact on commitment to independence is determined by ambiguity in both the exercise of authority by the internal auditor and deadline pressure faced by internal auditors combined with the discrepancy between the internal auditors' and managements' personal values.

Case study: Comparative Analysis of the Audit Committee's in UK and Egypt

To assess the similarities and differences of audit committees in UK and Egypt, a total of 6 companies and their annual reports were analysed. The companies reviewed were selected from high capitalisation indexes in the relative countries: The FTSE-100 for the UK and the EGX- 30 for Egypt (See Tables 1 and 2).

Table 1: FTSE all-share index ranking (as at close on Fri, 2 May 2014)

Rank	EPIC	Name	Index	Price	Mkt cap (m)
1	RDSA+RDSB	Royal Dutch Shell	FTSE 100	2,354.00 / 2,533.00	153,517.3
2	HSBA	HSBC Holdings	FTSE 100	605.70	114,051.1
3	BP.	BP	FTSE 100	501.70	95,619.2

Source: <http://www.stockchallenge.co.uk/ftse.php> retrieved on 08.05.2015

Table 2: EGX 30 Index (2014)

Rank	EPIC	Company Name		Index	Mkt cap (\$m)
1	OCI	Orascom Industries	Construction	EGX 30	8,783
2	CIB	Commercial Bank (Egypt)	International	EGX 30	4,759
3	OTH	Global Telecom Holding		EGX 30	3,975

Source: http://www.egyptse.com/index.asp?CurPage=EGX30_Overview.html, retrieved on 08.05.2015

These 6 companies were analysed by the factors listed in the next Table, for one year, namely 2013. The factors were chosen in order to draw the relevant conclusions dictated by the paper's introduction, research aims and objectives.

Table 3: Factors analysed

	Factors analysed
1	Size of Audit Committees
2	Number of AC meetings
3	Attendance of AC meetings
4	Standards followed by AC
5	Purpose of the AC
6	Relative Independence of AC

Audit Committee's Role and Responsibilities in UK

The companies analysed were: Royal Dutch Shell, HSBC Holdings and BP.

AC Role and Responsibilities

Royal Dutch Shell is an English company listed on the London Stock Exchange and is subject to the authority of the Financial Services Authority (FSA) in the United Kingdom. Consequently, Royal Dutch Shell follows the corporate governance principles set out in the UK Corporate Governance Code (the Code).

Purpose of the AC

The Committee (3 members) assists the Board of the Company in fulfilling its responsibilities in relation to risk management, internal control and financial reporting, and carries out certain oversight functions on behalf of the Board.

Table 4: The members of the AC at royal dutch shell

Chair:	Guy Elliott
Members:	Gerard Kleisterlee
	Linda G. Stuntz

Source: <http://www.hsbc.com/investorrelations/governance/board-committees>

Table 5: Attendance at meetings in 2013 at royal dutch shell

Name	Attended/Eligible to attend
Guy Elliott	6/6
Gerard Kleisterlee	5/6
Linda G. Stuntz	6/6

The purpose of the Audit Committee is to assist the Board of the Company (the "Board") in fulfilling its responsibilities in relation to internal control and financial reporting, and carries out certain oversight functions on behalf of the Board. Also, the Board is in full compliance with the requirements of the UK Corporate Governance Code. From the *Independence* point of view, all Committee members are designated by the Board as independent. Appointments of each Committee member are generally made for a period of up to three years, which may be extended for up to two further three-year periods in the case the members remain independent. All members are financially literate and at least one member qualifies as an "audit committee financial expert". According to the 2013 report, the AC has complied several duties:

Risk Management and Internal Control

- Review the policies and practices with respect to risk management and internal control.
- Monitor the effectiveness of the Group's risk management and internal control system, including in relation to material disputes, compliance and tax and information technology matters, make such recommendations as the Committee considers desirable and review the statements to be included in the annual reports concerning risk management and internal control.
- Monitor compliance with applicable external legal and regulatory requirements and the Code of Ethics for Executive Directors and Senior Financial Officers of the Shell Group.

Financial Reporting

- Discuss with the Chief Financial Officer, the Group Controller and the External Auditors issues regarding accounting policies and practices; the appropriateness and acceptability of judgements involving the application of accounting principles and
-

interpretation of applicable disclosure rules; and compliance with accounting and reporting standards required by law or supported by appropriate professional or other authorities.

- Review and discuss the integrity of annual audited Company financial statements and quarterly financial statements with management and the External Auditors.
- Establish and monitor the implementation of procedures for the receipt, retention and treatment of complaints regarding accounting, internal accounting controls, auditing or other matters, including mechanisms for the confidential or anonymous submission of related concerns by employees. The Committee shall also ensure that these procedures provide for proportionate and independent investigation of such matters and appropriate follow up action.
- Review the internal controls in relation to financial reporting, including related certification and attestation processes, monitor their effectiveness and make such recommendations as the Committee considers desirable.

Internal Audit

- Review and assess the internal audit function's remit, the appropriateness of internal audit strategies and the annual internal audit plan and, if satisfactory, recommend the same for approval by the Board. The Chief Internal Auditor shall have direct access to the Committee Chairman and to the Committee as a whole, and any member of the Committee shall also have direct access to the Chief Internal Auditor.
- Monitor the execution and results of the audit plan, material communications between the Chief Internal Auditor and the Company's management and any issues arising there from. The Committee shall review and assess management's response to audit findings and recommendations.
- Discuss the adequacy of the Company's risk management and internal control system and any significant matters arising from the internal audit with the Chief Internal Auditor, the Company's management and the External Auditors. Monitor the qualifications, expertise, resources, budget (and remuneration) and work structure of

the internal audit function, and review the same with the Chief Internal Auditor and with the External Auditors. The Committee shall consider, at least annually, the standards employed by the internal audit function, quality assurance procedures and auditor competence.

- Annually assess the performance of the Chief Internal Auditor, including the role and effectiveness of internal audit in the overall context of the Group's risk management and internal control system.

External Audit

Reporting

Other

HSBC Holdings

The *Group Audit Committee* (GAC) has non-executive responsibility for oversight of and advice to the Board on matters relating to financial reporting and for non-executive oversight of internal controls over financial reporting. The members of the GAC are John Coombe (Chairman), Marvin Cheung, Renato Fassbind and Rachel Lomax. All members of the Committee are independent non-executive Directors.

Table 6: The members of the GAC at HSBC holdings

Chair:	John Coombe
Members:	Marvin Cheung
	Renato Fassbind
	Rachel Lomax

Source: <http://www.hsbc.com/investorrelations/governance/board-committees>

HSBC is committed to high standards of corporate governance. During 2013 it has complied with the applicable code provisions of: (i) The UK Corporate Governance Code issued by the Financial Reporting Council; and (ii) the Hong Kong Corporate Governance Code.

Table 7: Attendance at meetings at HSBC holdings in 2013

Name	Attended/Eligible to attend
John Coombe	5/5
Marvin Cheung	5/5
Renato Fassbind	5/5
Rachel Lomax	2/2

BP

Table 8: Audit committee members at BP

Chairman:	Brendan Nelson
Members:	George David
	Phuthuma Nhleko
	Andrew Shilston

Table 9: Attendance at meetings in 2013 at BP

Name	Attended/Eligible to attend
George David ¹	12/12
Brendan Nelson ²	12/12
Phuthuma Nhleko ³	12/12
Andrew Shilston ⁴	11/12

Role of the Committee

The committee monitors the effectiveness of the group's financial reporting and systems of internal control and risk management.

Responsibilities

- Monitoring and obtaining assurance that the management or mitigation of financial risks are appropriately addressed by the group chief executive and that the internal control system is designed and implemented effectively in support of the limits imposed by the board ('Executive Limitations') as set out in the BP board governance principles;
- Reviewing financial statements and other financial disclosures and monitoring compliance with relevant legal and listing requirements;
- Reviewing the effectiveness of the group audit function and BP's internal financial controls and systems of internal control and risk management;
- Overseeing the appointment, remuneration, independence and performance of the external auditor and the integrity of the audit process as a whole, including the engagement of the external auditor to supply non-audit services to BP;
- Reviewing the systems in place to enable those who work for BP to raise concerns about possible improprieties in financial

¹¹ George David was unable to attend the Gulf of Mexico committee meeting on 8 March 2013 due to a clash with travel arrangements; he was unable to attend the chairman's committee meeting on

24 July 2013 due to a late change in the timing of the meeting

² Brendan Nelson attended all scheduled board meetings in 2013, however he was unable to attend the board teleconference on 21 February 2013 that was called at short notice due to a prior commitment with the Royal Bank of Scotland plc.

³ Phuthuma Nhleko was unable to attend the chairman's committee meeting on 24 July 2013 and the board meeting on 25 July 2013 due to unforeseen urgent family commitments

⁴ Andrew Shilston attended all scheduled board meetings in 2013, however he was unable to attend the two board teleconferences called at short notice on 16 January 2013 and 21 February 2013 due to prior commitments; he was unable to attend the audit committee meeting on 28 October 2013 due to major storms in the UK disrupting travel.

reporting or other issues and for those matters to be investigated⁵.

- The audit committee is made up of four members. The chairman used to be vice chairman of KPMG, is chairman of the group audit committee of The Royal Bank of Scotland Group plc, a member of the Financial Reporting Review Panel and president of the Institute of Chartered Accountants of Scotland and therefore holds recent and relevant financial experience as outlined in the UK Corporate Governance Code.

In 2013, BP's Audit committee Activities Involved

- Training
- Financial disclosure⁶
- Accounting judgements and estimates
- Audit committee focus
- Acquisitions of interests in other entities
- Taxation
- Derivative financial instruments
- Provisions and contingencies
- Gulf of Mexico oil spill
- Pensions and other post-retirement benefits
- Risk reviews⁷
- Internal control and risk management
- Auditor appointment and independence
- Audit tendering

Further on, we will focus only on the last three, which are more relevant for the current paper.

Internal Control and Risk Management

According to the 2013 report, the committee reviewed the group's system of internal

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<http://www.bp.com/en/global/corporate/investors/governance/board-performance-report-2013/board-committees/audit-committee-report/audit-committee-role-and-structure.html>, retrieved on 09.05.2014.

⁶ the committee reviewed the quarterly, half-year and annual financial statements with management, focusing on the integrity and clarity of disclosure, compliance with relevant legal and financial reporting standards and the application of critical accounting policies and judgments.

⁷ The group risks allocated to the audit committee for monitoring in 2013 included risks associated with trading activities, compliance with applicable laws and regulations and security threats against BP's digital infrastructure. For 2014, the board has agreed that the committee will maintain monitoring of the same group risks. The committee held in-depth reviews of these group risks over the year, examined succession planning and capability development in the finance function and reviewed the effectiveness and efficiency of the capital investment of a number of BP's major projects.

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control and risk management over the year, holding a joint meeting with the SEEAC to debate key audit findings and management's actions to remedy major problems.

The committee received quarterly reports on the findings of group audit, on identified fraud and misconduct and on key ethics and compliance issues. A further joint meeting with the SEEAC was held to discuss the annual certification report of compliance with the BP code of conduct. The two committees also met to discuss the group audit and ethics and compliance programmes for 2013. The committee held a private meeting with the group ethics and compliance officer during the year.

With regards to *auditor appointment and independence*, the committee's report takes into consideration only the external auditor.

As far as audit tendering is considered, during 2013, the committee considered the group's position on its audit services contract following changes to the UK Corporate Governance Code and proposed European Union regulations concerning the audit market. The committee examined a number of options regarding the timing of tendering for BP's external audit, including the mandatory rotation of the group's audit firm envisaged by proposed European regulations.

In view of the uncertainty regarding the form and impact of these regulations, the committee concluded that the best interests of the group and its shareholders would be served by utilizing the transition arrangements outlined by the FRC and retaining BP's existing audit firm until the conclusion of the term of its current lead partner. Accordingly the committee intends that the audit contract will be put out to tender in 2016, in order that a decision can be taken and communicated to shareholders at BP's AGM in 2017; the new audit services contract would then be effective from 2018.

Audit Committee's Role and Responsibilities in Egypt

The companies analysed were: Orascom Construction Industries, Commercial International Bank (Egypt) and Global Telecom Holding.

AC Role and Responsibilities

Orascom Construction Industries

The Company endeavours to observe and conducts its affairs in accordance with the Egypt Code of Corporate Governance and international corporate governance best practices⁸.

Audit Committee

The Audit Committee assists the Board in, among others, the oversight of both the internal and external audit functions. It receives its authority and its assignments from the Board which holds the final decision-making authority and action.

Table 10: Audit committee members at orascom construction industries

Chairman:	Claude Benmussa
Members:	Jean-Michel Thibaud
	Ahmed Bardai
	Khaled Bishara
	Hugues Foulon
	Aldo Mareuse

Source: <http://www.orascomci.com/>, retrieved on 12.05.2015.

Audit Committee Meetings

The Audit Committee meets at least four times per year (once each quarter), physically or via conference call, on a schedule adopted by the Committee, and as many additional times as deemed necessary.

During 2013, the Audit Committee held five meetings/conference calls. It also held a closed meeting with the external and internal auditors, i.e. without management.

Table 11: Audit committee members' attendance at orascom construction industries

Audit Committee Members	Attendance in person	Attendance by proxy	Attendance
Claude Benmussa ⁹	2	-	2/2
Jean-Michel Thibaud ¹⁰ (chairman)	5	-	5/5
Ahmed Barda	5	-	5/5
Aldo Mareuse	1	-	1/2
Khaled Bishara	3	-	3/3
Hugues Foulon ¹¹	3	-	3/3

⁸ <http://www.orascomci.com/filestore/AR2011.pdf>, retrieved on 12.05.2015.

⁹ Resigned on July 23, 2013

¹⁰ Appointed as AC Chairman on July 23, 2013

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Audit Committee Remuneration

ECMS Audit Committee members do not have a remuneration plan. However, at the Annual General Assembly held on March 22, 2013, the Shareholders approved an attendance fee per meeting and/or conference call.

Table 12: Audit committee remuneration at orascom construction industries

Audit Committee Attendance Fee for 2012	Description
Attendance fee for Chairman	EGP 25,000
Attendance fee per member / session	EGP 20,000□

Commercial International Bank (Egypt)

Table 13. Audit Committee Members at Commercial International Bank (Egypt)

Chairman:	Dr. Medhat Hassaneim
Members:	Sherif Kamel
	Yasser Hashem

Source: <http://www.cibeg.com/>, retrieved on 12.05.2015.

Table 14: Key responsibilities and members of the audit committee at commercial international bank (Egypt)

Audit Committee	Members	Key Responsibilities
Supervising the quality and integrity of CIB's financial reporting	Chair: Dr. Medhat Hassaneim Members: Dr. Sherif Kamel Mr. Yasser Hashem	Supervising the quality and integrity of CIB's financial reporting

The Committee's mandate is to ensure compliance with the highest levels of professional conduct, reporting practices, internal processes and controls. Consistent with the interests of all stakeholders, the Audit Committee also insists on high standards of transparency and strict adherence to internal policies and procedures.

Table 15: Audit committee members' attendance at commercial international bank (Egypt)

Audit Committee Members	Attendance in person	Attendance by proxy	Attendance
Medhat Hassaneim	3	-	3/6
Sherif Kamel	6	-	5/6
Yasser Hashem	6	-	6/6

¹¹ Appointed on July 23, 2013

In performing its critical functions, the Committee is cognizant of the important role CIB plays in the Egyptian financial sector as a leader in all of the aforementioned areas. The Audit Committee met six times in 2013.

Fiscal year 2013 was a period of productivity and major achievement for our Internal Audit function. We appreciate the strong and continuous support of the Board of Directors (BOD), Board Audit Committee and management team of CIB.

The Internal Audit Group (IAG) performs assurance engagements as a means of adding value, influencing changes that enhance Governance, Risk Management and Internal Control, as well as improving accountability for results. In 2013, IAG conducted 18 audit reports that covered several businesses units through an end-to-end process. These reports were presented to the BOD Audit Committee and CIB Management.

The Bank's Internal Audit function is adequately equipped to produce an independent and objective assurance to evaluate the adequacy and effectiveness of Governance, Risk Management, and Internal Control System. The IAG regularly tracks implementation of audit recommendations to ensure effectiveness.

Internal Audit undertakes a comprehensive risk-based audit approach over all of its audited business units, which is reflected in the three-year Audit Plan linked to CIB's strategy that covers the banking segments. The risk profile of each business function determines and identifies the number of internal audit visits to each business unit during the three- year plan cycle.

The Internal Audit function adopts the approach of business partners serving the BOD, Bank management and staff through providing consulting activities and participating as a non-voting member in most of the Bank's strategic committees without infringing on its independence.

To ensure the independence of the Audit function and in line with best corporate governance practices, Internal Audit has a

solid reporting line to the Board's Audit Committee.

The Committee reviews the efficiency of the Internal Control System to mitigate risks that threaten the achievement of the Bank's objectives and to ensure conformity with best practice and Institute of Internal Auditors (IIA) standards. The Committee also ensures the coordination between Audit, Risk Management, Internal Control and the Compliance department thus creating synergies and cost effectiveness.

Their Internal Audit team adds value by aggressively following up on and ensuring that Audit recommendations are properly considered and closed to mitigate risk-raised gaps. As for the fiscal year 2013, Internal Audit made 198 recommendations, of which 147 (74%) were properly resolved. The remaining 51 (26%) are in the pipeline waiting to be resolved by target dates that are coordinated with related business partners.

Internal Audit is concerned with the continuous education of its members, providing them with the support they need to qualify for certifications such as the CIA, CBA, CPA, CISA, and our in-house CIB Credit Course. Currently 30% of Internal Audit Staff are certified auditors with the remainder in the process of obtaining their respective certifications¹².

Therefore, the Audit Committee is composed of and chaired by Non-Executive Directors. The duties and responsibilities of this committee are in line with the Egyptian Capital Market Authority (CMA) regulations as well as the U.K. standards.

Global Telecom Holding

Table 16: Audit committee members at global telecom holding

Chairman:	Aladdin Saba
Members:	Alex Shalaby
	Mohamed Shaker

Source: <http://www.gtelecom.com/web/guest/audit-committee>

¹²

<http://www.cibeg.com/English/InvestorRelations/FinancialInformation/Annual%20Reports/CIB%20Annual%20Report%202013.pdf>

The Committee is responsible for assisting the Board of Directors in fulfilling its oversight responsibilities for the integrity of the Company's:

- Accounting and financial reporting process,
- System of internal control over financial reporting,
- System of disclosure controls and procedures,
- Audit process and,
- Process for monitoring compliance with the best practice and the CMA listing applicable laws and regulations.

Table 17: Attendance at meetings in 2013 at global telecom holding

Name	Attended/Eligible to attend
Aladdin Saba	4
Alex Shalaby	4
Mohamed Shaker	4

The Audit Committee interacts directly with the independent auditor to ensure the independent auditor is ultimate accountability to the Board and the Committee, as representatives of the shareholders, and is directly responsible for the appointment, compensation and oversight of the independent auditor¹³.

Research Findings and Conclusions

Following the rationale already outlined above, the two countries analysed were chosen for their representation of prevalent AC structures. This is to better analyse audit committees in their international and functional context.

Size of Audit Committees

Table 18: AC structures by country

UK	AC members	Egypt	AC members
Royal Dutch Shell	3	Orascom Construction Industries	6
HSBC Holdings	4	Commercial International Bank (Egypt)	3
BP	4	Global Telecom Holding	3
Average	3.66		4

The table above clearly shows the makeup of the AC structures in Egypt and the United Kingdom. According to this information, the Size of Audit Committees by Country, shows

that the 3-companies average size of audit committees is 3.66 members in the UK and 4 members in Egypt. It seems that Egypt has the larger audit committee size in the entity of Orascom Construction Industries. Higher size can be explained by the perceived relative importance of audit committees in both countries.

Number of AC Meetings

Table 19: Number of AC meetings

UK	AC members	Egypt	AC members
Royal Dutch Shell	6	Orascom Construction Industries	5
HSBC Holdings	5	Commercial International Bank (Egypt)	6
BP	12	Global Telecom Holding	4
Average	7.66		5

The table above clearly shows the number of AC meetings in Egypt and the United Kingdom. According to this information, the AC meetings by Country show that the 3-companies average meeting attendance of audit committees members is 7.66 (meetings) in the UK and 4 (meetings) in Egypt. It seems that UK has more often meetings than the Egyptian companies, probably because the companies from UK pay more attention to AC and corporate governance. Higher number of attendances can be explained by the perceived relative importance of audit committees in UK.

Attendance of AC Meetings

As for the attendance of AC meetings, it can be seen that the percentage of attendance reaches 97% in UK companies, meanwhile in the Egyptian companies it hardly reaches 84.3%, as in the table below.

Table 20: Attendance of AC meetings

UK	Attendance of AC meetings	Egypt	Attendance of AC meetings
Royal Dutch Shell	93%	Orascom Construction Industries	76%
HSBC Holdings	100%	Commercial International Bank (Egypt)	77%
BP	98%	Global Telecom Holding	100%
Average	97%		84.3%

This signifies that in the UK, the IAF, AC and CG are taken seriously and that the

¹³

<http://www.gtelecom.com/documents/10157/24707/Global+Telecom+-+2012+Annual+Report.pdf>

major role of AC in CG is well recognised. In Egypt, there is still some way to go to reach this manner of thinking.

Standards followed by AC

The Boards of the analysed companies are in full compliance with the requirements of the UK Corporate Governance Code. In addition, HSBC is committed to high standards of corporate governance. During 2013 it has complied with the applicable code provisions of: (i) The UK Corporate Governance Code issued by the Financial Reporting Council; and (ii) the Hong Kong Corporate Governance Code.

The companies from Egypt have AC duties and responsibilities in line with the Egyptian Capital Market Authority (CMA) regulations as well as with the U.K. standards.

Purpose of the AC

In the UK, as seen in our analysis, generally, the Audit Committee assists the Board of the Company in fulfilling its responsibilities in relation to risk management, internal control and financial reporting, and carries out certain oversight functions on behalf of the Board. This means high responsibilities since the major goals are similar to those of CG. The purpose of the Audit Committee is to assist the Board of the Company (the "Board") in fulfilling its responsibilities in relation to internal control and financial reporting, and carries out certain oversight functions on behalf of the Board. Other way round, the committees monitor the effectiveness of the groups' financial reporting and systems of internal control and risk management.

At the same time, during 2013, BP Audit committee proposed European Union regulations concerning the audit market, this meaning that the company is interested and careful to all new regulations, also trying to participate to them.

With regards to the Egyptian companies, generally, the Audit Committee assists the Board in, among others, the oversight of both the internal and external audit functions. It receives its authority and its assignments from the Board which holds the final

decision-making authority and action. Also, the Committee's mandate is to ensure compliance with the highest levels of professional conduct, reporting practices, internal processes and controls. Consistent with the interests of all stakeholders, the Audit Committee also insists on high standards of transparency and strict adherence to internal policies and procedures.

Relative Independence of AC

From the *Independence* point of view, all Committee members of the analysed companies from UK are designated by the Board as independent. This can be attributed to the fact that most NEDs in the UK are independent to begin with. In Egypt, as well, the AC is composed of non-executive directors or Independent Directors. Also, in order to ensure the independence of the Audit function and in line with best corporate governance practices, Internal Audit has a solid reporting line to the Board's Audit Committee. Usually, the Committee reviews the efficiency of the Internal Control System to mitigate risks that threaten the achievement of the firm's objectives and to ensure conformity with best practice and Institute of Internal Auditors (IIA) standards [38-40].

Conclusions

To summarise the findings, it can be said that the both in UK and Egypt, the role of AC and IA in CG is highly admitted and recognized. Thus, from an *independence perspective*, both the UK and the Egyptian audit committees are completely independent, the Board focusing very much on ensuring the independence of the Audit function which usually tends to be in line with best corporate governance practices. At the same time, in both countries, Internal Audit has a solid reporting line to the Board's Audit Committee. In addition, in both countries, the Audit Committee Members should be and therefore are all non-executives in accordance with the Stock Exchange Listing Rules, with no membership in any other Board Committees. We can therefore conclude that the Audit Committee is structured to ensure independence and integrity.

As far as the standards are concerned, all the corporations from UK respect the Corporate Governance Code issued by the Financial Reporting Council, meanwhile in the corporations from Egypt the Audit Committee conducts audit in accordance with the Egyptian Standards on Auditing and in the light of the prevailing Egyptian laws.

As for differences, companies from UK have the biggest number of audit committee meetings attendance, meanwhile the Egyptian companies do not have such a high ratio attendance of committee meetings.

Within a smaller, nimbler, less regulated unitary board structure such as the UK,

audit committees are seen as cornerstones of corporate governance and internal control. In larger, co-determined, regulated two-tier board structures such as Egypt, audit committees are seen as ancillary to the already existent governance functions of the supervisory board.

The UK scope, range, independence and purpose of audit committees as per legislation and practice, is substantially larger than those of Egypt. Most probably, the earlier adoption of a committee structure, the nimbler structure of boards and the lighter regulatory approach in the UK clearly contribute to this. However, audit committees are one form corporate governance and control both in UK and Egypt.

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