

**PRA RULEBOOK: CRR FIRMS AND SOLVENCY II FIRMS: AUDIT COMMITTEE INSTRUMENT  
2016**

**Powers exercised**

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137G (the PRA’s general rules); and
  - (2) section 137T (general supplementary powers).
- B. The rule-making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

**Pre-conditions to making**

- C. In accordance with section 138J of the Act (Consultation by the PRA), the PRA consulted the Financial Conduct Authority. After consulting, the PRA published a draft of proposed rules and had regard to representations made.

**PRA Rulebook: CRR Firms and Solvency II Firms: Audit Committee Instrument 2016**

- D. The PRA makes the rules in the Annex to this instrument.

**Commencement**

- E. This instrument comes into force on 17 June 2016.

**Citation**

- F. This instrument may be cited as the PRA Rulebook: CRR Firms and Solvency II Firms: Audit Committee Instrument 2016.

**By order of the Board of the Prudential Regulation Authority**

10 May 2016.

## **Annex**

In this Annex, the text is all new and is not underlined.

**Part**

# **AUDIT COMMITTEE**

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## 1 APPLICATION AND DEFINITIONS

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1.1 Unless otherwise stated, this Part applies to:

- (1) a *CRR firm*;
- (2) a *UK Solvency II firm*;
- (3) in accordance with Insurance General Application 3, the *Society*, as modified by 3; and
- (4) in accordance with Insurance General Application 3, *managing agents*, as modified by 3.

1.2 This Part does not apply to a *firm* which is a *subsidiary undertaking* of an EEA *parent undertaking* where the *parent undertaking* complies at group level with Chapter 2 or with requirements implementing Article 39 of the *Statutory Audit Directive* in any other EEA State and, where applicable, with Articles 11(1), 11(2) and 16(5) of the *Statutory Audit Regulation*, provided that:

- (1) the *firm* is not significant; or
- (2) if the *firm* is significant, its *governing body* is composed of the same *non-executive directors* as the *governing body* of that *parent undertaking*.

**[Note: Art. 39(3)(a) (part) of the *Statutory Audit Directive*]**

1.3 This Part applies to a *firm* in respect of financial years beginning on or after 17 June 2016.

1.4 In this Part, the following definitions shall apply:

*aggregate accounts*

means the aggregate accounts required to be prepared by the *Council* under regulation 18 of the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 (SI 2008/1950).

*audit committee*

means a committee established in accordance with 2.1.

*Statutory Audit Directive*

means Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC.

*Statutory Audit Regulation*

means Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC.

*syndicate statutory accounts*

means the *syndicate's* annual accounts and underwriting year accounts for a financial year prepared under regulations 5(2)(a) and 6(1) of the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 (SI 2008/1950).

## 2 AUDIT COMMITTEE

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2.1 Subject to 2.3, a *firm* must have an *audit committee* which meets the criteria set out in 2.2 and which is responsible for performing the functions set out in 2.4.

**[Note: Art. 39(1) (part) of the Statutory Audit Directive]**

2.2 The criteria referred to in 2.1 are:

- (1) the *audit committee* must be a committee of the *governing body* of the *firm*;
- (2) the *audit committee* must be composed only of *non-executive directors*;
- (3) at least one member of the *audit committee* must have competence in accounting and/or auditing;
- (4) the members of the *audit committee* as a whole must have competence relevant to the sector in which the *firm* is operating;
- (5) a majority of the members, including the chairman, of the *audit committee* of a *firm* must be independent of the *firm* provided that:
  - (a) the *firm* is not significant; or
  - (b) the *firm* is a significant *subsidiary undertaking* of a *parent undertaking* and all members of the *parent undertaking's audit committee* are independent of the *parent undertaking*;
- (6) subject to (5)(b), all members of the *audit committee* of a *firm* that is significant must be independent of the *firm*; and
- (7) the chairman of the *audit committee* must be appointed by its members and must be independent of the *firm*.

**[Note: Art. 39(1) (part) of the Statutory Audit Directive]**

2.3 A *firm* may combine its *audit committee* with its risk committee (if applicable) provided that:

- (1) the *firm* is not significant; and
- (2) the members of the combined committee have the knowledge, skills and expertise required for the exercise of the functions of the risk committee and the *audit committee*.

**[Note: Art. 76(3) CRD]**

- 2.4 A *firm* must ensure that its *audit committee* performs at least the following functions:
- (1) informs the *governing body* of the *firm* of the outcome of the statutory audit and explains how the statutory audit contributed to the integrity of financial reporting and what the role of the *audit committee* was in that process;
  - (2) monitors the financial reporting process and submits recommendations or proposals to ensure its integrity;
  - (3) monitors the effectiveness of the *firm's* internal quality control and risk management systems and, where applicable, its internal audit, regarding the financial reporting of the *firm*, without breaching its independence;
  - (4) monitors the statutory audit of the annual and consolidated financial statements, in particular, its performance, taking into account, where applicable, any findings and conclusions of the Financial Reporting Council Limited pursuant to Article 26(6) of the *Statutory Audit Regulation*;
  - (5) reviews and monitors the independence of the statutory auditor or the audit firm in accordance with, where applicable, paragraphs 2(3), 2(4), 3, 4(1), 4(2), 5 to 8 and 10 to 12 of Schedule 1 to the Statutory Auditors and Third Country Auditors Regulations 2016 (SI 2016/XXX) and, where applicable, Article 6 of the *Statutory Audit Regulation*, and in particular the suitability of the provision of non-audit services to the *firm* in accordance with Article 5 of the *Statutory Audit Regulation*; and
  - (6) is responsible for the procedure for the selection of the statutory auditor or audit firm and recommends the statutory auditor or the audit firm to be appointed, where applicable, in accordance with Article 16 of the *Statutory Audit Regulation*, except when Article 16(8) of the *Statutory Audit Regulation* is applied.

**[Note: Art. 39(6) of the Statutory Audit Directive]****3 LLOYD'S**

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- 3.1 This Part applies to the *Society* and *managing agents* separately.
- 3.2 For the purposes of complying with 2, a *managing agent* must establish an *audit committee* which meets the criteria set out in 2.2 and which is responsible for performing the functions set out in 2.4 in respect of:
- (1) each *syndicate* it manages; and
  - (2) any *syndicate* in respect of which it was the last *managing agent* to manage during the preceding year and which has no *managing agent* on 31 December where *syndicate statutory accounts* are required to be prepared.
- 3.3 For the purpose of:
- (1) 2, as applied to the *Society*, references to “*governing body*” are to be interpreted as references to the *Council*.

- (2) 2.4, as applied to *managing agents*,
  - (a) references to “statutory audit” and “statutory audit of the annual and consolidated financial statements” are to be interpreted as references to the audit of the *syndicate statutory accounts* in accordance with the requirements of the Insurance Accounts Directive (Lloyd’s Syndicate and Aggregate Accounts) Regulations 2008 (SI 2008/1950); and
  - (b) references to “statutory auditor” or “audit firm” are to be interpreted as a reference to the statutory auditor or audit firm responsible for the audit of the *syndicate statutory accounts* referred to in 3.3(2)(a);
- (3) 2.4(3), as applied to *managing agents*, the reference to “the financial reporting of the *firm*” is to be interpreted as a reference to the financial reporting in respect of each *syndicate* referred to in 3.2 for which the *managing agent* is responsible; and
- (4) 2.4, as applied to the *Society*,
  - (a) references to “statutory audit” and “statutory audit of the annual and consolidated financial statements” are to be interpreted as references to the audit of the *aggregate accounts* in accordance with the requirements of the Insurance Accounts Directive (Lloyd’s Syndicate and Aggregate Accounts) Regulations 2008 (SI 2008/1950) and the audit of the *Society’s* group financial statements; and
  - (b) references to “statutory auditor” or “audit firm” are to be interpreted as references to the auditor or audit firm responsible for the audit of the *aggregate accounts* referred to in 3.3(4)(a) and the audit of the *Society’s* group financial statements.

#### 4 TRANSITIONAL PROVISIONS

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- 4.1 2.2 (6) shall not apply until the commencement of a *firm’s* financial year beginning on or after 17 June 2018 provided that a majority of the members, including the chairman, of the *audit committee* of a significant *firm* are independent of the *firm*.
- 4.2 Subject to 4.3, a *firm* that is not significant or is a *subsidiary undertaking* of a non-EEA *parent undertaking* may not have an *audit committee* until the commencement of a *firm’s* financial year beginning on or after 17 June 2018 if its *governing body* is performing equivalent functions to an *audit committee*. In such a case 2.2 (1), 2.2 (2), 2.2 (5), 2.2 (6) and 2.2 (7) shall not apply, and the *firm* must disclose that the *governing body* carries out the *audit committee’s* functions and how its *governing body* is composed.
- 4.3 Until the commencement of a *firm’s* financial year beginning on or after 17 June 2018, where all members of the *audit committee* are members of the *governing body* of a *firm* that is not significant or is a *subsidiary undertaking* of a non-EEA *parent undertaking*, the *audit committee* is to be exempt from the independence requirements laid down in 2.2 (5), 2.2 (6) and 2.2 (7).
- 4.4 Chapter 2 shall not apply to a significant *firm* which is a *subsidiary undertaking* of an EEA *parent undertaking* until the commencement of a *firm’s* financial year beginning on or after 17

June 2018, where the *parent undertaking* complies at group level with Chapter 2 or with requirements implementing Article 39 of the *Statutory Audit Directive* in any other EEA State and, where applicable, with Articles 11(1), 11(2) and 16(5) of the *Statutory Audit Regulation*.