

# REPORT OF THE AUDIT COMMITTEE

As Chairman of the Audit Committee, I am pleased to present the report of the committee for the year ended 31 December 2016.

This report details how the Audit Committee has met its responsibilities under its Terms of Reference and under the 2014 UK Corporate Governance Code in the last twelve months.

The Audit Committee focused particularly on the appropriateness of the Group's financial statements. The committee has satisfied itself, and has advised the Board accordingly, that the 2016 Annual Report and financial statements are fair, balanced and understandable, and provide the information necessary for shareholders to assess the Company's performance, business model and strategy. The significant issues that the committee

considered in relation to the financial statements and how these issues were addressed are set out in this Report.

The Audit Committee notes the new requirements under section 225 of the Companies Act 2014 and has ensured that the Directors are aware of their responsibilities and fully comply with this provision.

One of the Audit Committee's key responsibilities is to review the Group's risk management and internal controls systems, including in particular internal financial controls. During the year, the committee carried out a robust assessment of the principal

risks facing the company and monitored the risk management and internal control system on an on-going basis. Further details in regard to these matters are also set out in this Report on page 77.

The committee also reviewed the effectiveness of both the external audit process and the internal audit function as part of the continuous improvement of financial reporting and risk management across the Group.

**Michael Cawley**  
Chairman,  
Audit Committee



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## ROLE AND RESPONSIBILITIES

The Board has established an Audit Committee to monitor the integrity of the Company's financial statements and the effectiveness of the Group's internal financial controls. The committee's role and responsibilities are set out in the committee's terms of reference which are available from the Company and are displayed on the Group's website ([www.kingspan.com](http://www.kingspan.com)). The Terms of Reference are reviewed annually and amended where appropriate. During the year the committee worked with management, the external auditors, internal audit, and other members of the senior management team in fulfilling these responsibilities.

The Audit Committee report deals with the key areas in which the Audit Committee plays an active role and has responsibility. These areas are as follows:

- Financial Reporting and related primary areas of judgement;
- The External Audit process;
- The Group's Internal Audit function
- Risk Management and Internal controls; and
- Whistleblowing procedures.

## COMMITTEE MEMBERSHIP

As at 31 December 2016, the Audit Committee comprised of three independent non-executive Directors who are Michael Cawley (Chairman), Linda Hickey and John Cronin.

The biographies of each can be found on pages 44 and 45.

The Board considers that the committee as a whole has an appropriate and experienced blend of commercial, financial and industry expertise to enable it to fulfil its duties, and that the committee chairman, Michael Cawley B.COMM., F.C.A., has appropriate recent and relevant financial experience.

## MEETINGS

The committee met four times during the year ended 31 December 2016 and attendance at the meetings is noted below. The activities of the Audit Committee in each meeting are noted on the page below.

Committee Member	Attended	Eligible	Joined Committee
Michael Cawley (Chairman)	4	4	2014
Linda Hickey	4	4	2013
John Cronin	4	4	2015

Audit Committee activities	Feb	June	Aug	Dec
<b>Financial reporting</b>				
Review and approve preliminary & interim results	•		•	
Consider key audit and accounting issues and judgements	•		•	
Consider accounting policies and the impact of new accounting standards	•		•	
Review any related party matters and intended disclosures	•			
Review management letter from auditors	•			
Approve going concern and viability statements	•			
Review Annual Report, and confirm if fair balanced and understandable	•			
<b>External auditors</b>				
Plan for year-end audit & half year review		•		•
Confirm auditor independence, materiality of fees, and non-audit services		•		•
Approval of audit engagement letter and audit fees				•
<b>Internal audit and risk management controls</b>				
Approve internal audit plan and resources	•	•	•	•
Review of internal audit reports and monitor progress on open actions	•	•	•	•
Review of financial, IT and general controls	•	•	•	•
Monitor Group whistleblowing procedures	•	•	•	•
Assessment of the principal risks and effectiveness of internal control systems				•
<b>Governance</b>				
Assurances as to corporate governance and Corporate Governance Code compliance	•			
Accounting standards update		•		•
Corporate governance update		•		•
Evaluation of external and internal audit function		•		
Directors' Compliance Statement policy and procedures				•
Policy on the engagement of external auditors				•

Each committee meeting was attended by the Group Chief Financial Officer, the Group Financial Controller and the Head of Internal Audit. The external auditors also attended these meetings as required. The Company Secretary is the secretary of the Audit Committee. Other Directors can attend the meetings as required.

The chairman of the Audit Committee also met with both the Head of Internal Audit and the external audit lead partner outside of committee meetings as required throughout the year.

#### COMMITTEE EVALUATION

As outlined on page 57 within the Corporate Governance Statement, the performance of the Board also includes a review of the Committees. Any recommendations raised in relation to the Audit Committee are acted upon in a formal and structured manner. No issues were identified for the year ending 31 December 2016.

#### FINANCIAL REPORTING

The committee is responsible for monitoring the integrity of the Group's financial statements and reviewing the financial reporting judgements contained therein. The financial statements are prepared by a finance team with the appropriate qualifications and expertise.

The Committee confirmed to the Board that the annual report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy.

In respect of the year to 31 December 2016, the committee reviewed:

- › the Group's Interim Management Statements issued in May and November 2016;
- › the Group's Interim Report for the six months to 30 June 2016; and
- › the Preliminary Announcement and Annual Report to 31 December 2016.

In carrying out these reviews, the committee:

- › reviewed the appropriateness of Group accounting policies and monitored changes to and compliance with accounting standards on an on-going basis;
- › discussed with management and the external auditors the critical accounting policies and judgements that had been applied;
- › compared the results with management accounts and budgets, and reviewed reconciliations between these and the final results;

- › discussed a report from the external auditors at that meeting identifying the significant accounting and judgemental issues that arose in the course of the audit;
- › considered the management representation letter requested by the auditors for any non-standard issues and monitored action taken by management as a result of any recommendations;
- › discussed with management future accounting developments which are likely to affect the financial statements;
- › reviewed the budgets and strategic plans of the Group in order to ensure that all forward looking statements made within the Annual Report reflect the actual position of the Group; and
- › considered key areas in which estimates and judgement had been applied in preparation of the financial statements including, but not limited to, a review of fair values on acquisition, the carrying amount of goodwill, intangible assets and property, plant and equipment, litigation and warranty provisions, recoverability of trade receivables, valuation of inventory, hedge accounting treatments, treasury matters and tax matters.

The primary areas of judgement considered by the committee in relation to the Group's 2016 financial statements, and how they were addressed by the committee are set out below.

Each of these areas received particular focus from the external auditor, who provided detailed analysis and assessment of the matter in their report to the committee.

In addition, the internal audit team review the businesses covered in their annual Internal Audit Plan, as agreed by the committee, and report their findings to the Audit Committee throughout the year. These internal audit reviews are focused on areas of judgement such as warranty provisions, trade receivables and inventory and provide the committee information on the adequacy and appropriateness of provisions in these areas.

Primary areas of judgement	Committee activity
<b>Consideration of impairment of goodwill</b>	<p>The committee considered the annual impairment assessment of goodwill prepared by management for each Cash Generating Unit ("CGU") using a discounted cash flow analysis based on the strategic plans approved by the Board, including a sensitivity analysis on key assumptions. The primary judgement areas were the achievability of the long term business plans and the key macroeconomic and business specific assumptions. In considering the matter, the committee discussed with management the judgements made and the sensitivities performed. Further detail of the methodology is set out in Note 9 to the financial statements.</p> <p>KPMG also provided the Committee with their evaluation of the impairment review process. Kingspan completed 6 acquisitions during the financial year. The allocation of goodwill to CGUs is not yet complete for all acquisitions but the methodology of the assessments of such items of goodwill was presented to the Committee and the results were deemed appropriate.</p>
<b>Adequacy of warranty provision</b>	<p>The committee reviewed the judgements applied by management in assessing both specific and risk based warranty provision at 31 December 2016. The committee reviewed and discussed with management the monthly reports presented to the Board which set out, for each of the Group's divisions, warranty provision and warranty costs and analyse these costs as a percentage of divisional sales. A retrospective review of warranty provision at 31 December 2015 was also carried out in order to note any indication of management bias within the provisions and none was noted. The Committee was satisfied that such judgements were appropriate and the risk had been adequately addressed.</p>
<b>Recoverability of trade receivables and adequacy of provision</b>	<p>The committee reviewed the judgements applied by management in determining the bad debt provision at 31 December 2016. The committee reviewed and discussed with management the monthly Board report which sets out aged analysis of gross debtor balances and associated bad debt provision and reviewed security (including credit insurance) that is in place. A retrospective review of bad debt provision at 31 December 2015 was also carried out in order to note any indication of management bias within the provision and none was noted. The Committee was satisfied that such judgements were appropriate and the risk had been adequately addressed.</p>
<b>Valuation of inventory and adequacy of inventory provision</b>	<p>The committee reviewed the valuation and provisioning for inventory at 31 December 2016. The main area of judgement was the level of provisioning required for slow moving and obsolete inventory. The committee reviewed and discussed with management the monthly board report which sets out, for each of the Group's divisions, gross inventory balances and associated obsolescence provision including an analysis by inventory, category and ageing. A retrospective review of the inventory provision at 31 December 2015 was also carried out in order to note any indication of management bias within the provisions and none was noted. The Committee was satisfied that such judgements were appropriate and the risk had been adequately addressed.</p>
<b>Taxation</b>	<p>Provisioning for potential current tax liabilities and the level of deferred tax asset recognition in relation to accumulated tax losses are underpinned by a range of judgements. The committee addresses these issues through a range of reporting from senior management and a process of challenging the appropriateness of management's views including the degree to which these are supported by professional advice from external legal and other advisory firms.</p> <p>The Group's accounting manual sets out detailed policies that prescribe the methodology to be used by management in calculating the above provisions. Each division formally confirms compliance with these policies on an annual basis.</p> <p>The Committee was satisfied that such judgements were appropriate and the risk had been adequately addressed.</p>
<b>Accounting for acquisitions</b>	<p>Total acquisition consideration in 2016 amounted to €262.4m, including deferred contingent consideration and transfer of assets. The committee discussed with management and the external auditors the accounting treatment for newly acquired businesses, and the related judgements made by management, and were satisfied that the treatment in the Group's financial statements was appropriate.</p>

## EXTERNAL AUDITOR

The Audit Committee has responsibility for overseeing the Group's relationship with the external auditor including reviewing the quality and effectiveness of their performance, their external audit plan and process, their independence from the Group, their appointment and their audit fee proposals.

### Performance and audit plan

Following the completion of the 2015 year-end audit, the committee carried out a review of the effectiveness of the external auditor and the audit process. This review involved discussions with both group management and internal audit and feedback provided by divisional management. The committee continues to monitor the performance and objectivity of the external auditors and takes this into consideration when making its recommendations to the Board on the remuneration, the terms of engagement and the re-appointment, or otherwise, of the external auditors.

Prior to commencement of the 2016 year-end audit and half-year review, the committee approved the external auditor's work plan and resources and agreed with the auditor's various key areas of focus, including accounting for acquisitions, impairments, warranty provisions, as well as a particular focus on certain higher risk jurisdictions.

During the year the committee met with the external auditor without management being present. This meeting provided the opportunity for direct dialogue and feedback between the committee and the auditor, where they discussed inter alia some of the key audit management letter points.

### EU Audit Reform

EU legislation providing a new regulatory framework for statutory audit was adopted in April 2014 (comprising Directive 2014/56/EU and Regulation EU No. 537/2014). EU Audit reform legislation is applicable in the Member States of the European Union, including Ireland, and is applicable for the first financial year that commences after 17 June 2016. Under this legislation, Kingspan Group plc is considered a Public Interest Entity ("PIE"). The key

changes arising from the implementation of this legislation are:

- › a requirement that the PIE changes its statutory auditor at least every ten years (following rotation, the statutory audit firm cannot be reappointed for four years);
- › a requirement that certain procedures are followed for the selection of the new statutory auditor; and
- › restrictions on the entitlement of the statutory auditing firm to provide certain non-audit services.

Kingspan Group plc will be in full compliance with such EU Audit Reform from the period commencing 1 January 2017. With regards audit firm rotation, at the very latest, KPMG will be in situ for the final time for the year ending 31 December 2020 and thereafter a formal tender process will commence.

### Independence and objectivity

The committee is responsible for ensuring that the external auditor is objective and independent. KPMG has been the Group's auditor since 2011, following a formal tender process in which a number of leading global firms submitted written tenders and presentations. This was the last formal tender process carried out by the Group. The lead audit partner is rotated every five years. During 2016, David Meagher succeeded Roger Gillespie as lead audit partner.

The committee received confirmation from the auditor that they are independent of the Group under the requirements of the Financial Reporting Council's Ethical Standards for Auditors. The auditors also confirmed that they were not aware of any relationships between the Group and the firm or between the firm and any persons in financial reporting oversight roles in the Group that may affect its independence.

### Non-audit services

In order to further ensure independence, the committee has a policy on the provision of non-audit services by the external auditor that seeks to ensure that the services provided by the external auditor are not, or are not perceived to be, in conflict with auditor independence. By obtaining an account of all relationships between the external auditor and the Group, and by reviewing the economic importance of the Group to the external auditor by monitoring the audit fees as a percentage of total income generated from the relationship with the Group, the committee ensured that the independence of the external audit was not compromised. During the year the committee reviewed and updated its policy on the engagement of external auditors and the provision of non-audit services in order to bring it into full compliance with the EU audit reform legislation. An analysis of fees paid to the external auditor, including non-audit fees, is set out in Note 5 and detailed below:

### Audit V Non Audit Services Remuneration



## INTERNAL AUDIT

The committee reviewed and agreed the annual internal audit plan, which the committee believes is appropriate to the scope and nature of the Group. The internal audit plan is risk based, with all divisions audited every year, and all new businesses audited within 12 months of acquisition.

The committee reviewed reports from the Head of Internal Audit at its quarterly meetings. These reports enable the committee to monitor the progress of the internal audit plan, to discuss key findings and the plan to address them in addition to status updates of previous key findings.

The committee is responsible for reviewing the effectiveness of the internal audit function and does so based upon discussion with Group management, the Group's external auditor and feedback provided by divisional management. The committee was satisfied that the internal audit function is working effectively, improves risk management throughout the Group and that the internal audit function team is sufficiently resourced in addition to having the adequate level of experience and expertise.

### RISK MANAGEMENT AND INTERNAL CONTROLS

The Audit Committee has been delegated, from the Board, the responsibility for monitoring the effectiveness of the Group's system of risk management and internal control.

The Audit Committee monitors the Group's risk management and internal control processes through detailed discussions with management and executive Directors, the review and approval of the internal audit reports, which focus on the areas of greatest risk to the Group, and the external audit reports, as part of both the year-end audit and the half year review process, all of which highlight the key areas of control weakness in the Group. All weaknesses identified by either internal or external audit are discussed by the committee with Group management and an implementation plan for the targeted improvements to these systems is put in place. The implementation plan is being overseen by the Group Chief Financial Officer and the committee

is satisfied that this plan is being properly executed.

As part of its standing schedule of business, the committee carried out an annual risk assessment of the business to formally identify the key risks facing the Group. Full details of this risk assessment and the key risks identified are set out in the Risk & Risk Management section of this Annual Report on pages 30 and 31.

These processes, which are used by the Audit Committee to monitor the effectiveness of the Group's system of risk management and internal control, are in place throughout the accounting period and remain in place up to the date of approval of this Annual Report.

The main features of the Group's internal control and risk management systems that specifically relate to the Group's financial reporting and accounts consolidation process are set out in the Corporate Governance Report on page 60.

### WHISTLEBLOWING PROCEDURES

The Group has a Code of Conduct, full details of which are available on the Group's website ([www.kingspan.com](http://www.kingspan.com)).

Based on the standards set out in this Code of Conduct, the Group employs a comprehensive, confidential and independent whistleblowing phone service to allow all employees raise their concerns about their working environment and business practices. This service then allows management and employees to work together to address any instances of fraud, abuse and other misconduct in the workplace.

Any instances of fraud, abuse or misconduct reported on the whistleblowing phone service are reported to the Head of Internal Audit and the Company Secretary, who then evaluate each incident for onward communication to the committee. This onwards communication consists of the full details of the incident, key control failures, any financial loss and actions for improvement.

During the year, the committee reviewed the Group's whistleblowing process and were satisfied with the design and operating effectiveness of the process.



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Kooltherm Pitched Roof Board