

Audit and Risk Committee Report

Chair



Frank Nelson

Members



Martyn Coffey



Sucheta Govil

Dear Shareholder,

I am pleased to report to you on the Audit and Risk Committee's objectives and activities during 2019.

This report, which is part of the Directors' Report, explains how the Audit and Risk Committee has discharged its responsibilities during 2019, and reflects the recent changes to reporting under the Code. I hope you find it useful and informative.

During the year, in addition to its routine reviews of external financial reporting, the Committee has received regular progress updates on the Group's implementation of the new lease accounting standard IFRS 16 which is applicable for the first time in 2019. I am pleased to note the Group's adoption, in conjunction with the external auditors, has been performed smoothly.

In accordance with best ethical standards, and PwC LLP's partner rotation policy, I can confirm the current audit engagement partner will step-down following the 2019 audit, after five years of client service to Eurocell. On behalf of the Committee, I would like to thank Mark Smith for his contribution and for the transitional arrangements which are in place for his successor.

In-line with best practice, an externally-facilitated review of the Committee's effectiveness was concluded this year and I am pleased to report that no significant areas of concern were identified and the Committee was viewed as operating effectively.

Finally, I would like to thank my fellow Committee members, all of whom have served throughout the year, for their valuable contribution and support, and I welcome any comments or questions from shareholders.

Frank Nelson

Chair of the Audit and Risk Committee
12 March 2020

Role and responsibilities:

The key responsibilities of the Committee are to:

- review the Annual Report, half-year report and any other formal announcements relating to the Group's financial performance, giving due consideration to significant accounting issues and judgements contained therein, as well as compliance with accounting standards and other legal and regulatory requirements;
- review the Annual Report and Financial Statements to advise the Board on whether they give a fair, balanced and understandable explanation of the Group's business and performance over the relevant period;
- review the Group's financial reporting systems and procedures;
- review the Group's internal controls and risk management systems and advise the Board whether they are adequate, by considering reports on their effectiveness from the Chief Financial Officer and Chief Executive Officer, together with reports from the Group's outsourced internal auditor and from the external auditor;
- review and update the Group's risk register, as part of the assessment of emerging and principal risks;
- review the Group's procedures to ensure compliance with the provisions of the Bribery Act 2010 and the Group's whistleblowing policy;
- review the external auditor's independence and objectivity, audit and non-audit fees and make recommendations regarding audit tender and the appointment and remuneration of the auditor, together with the terms of their engagement;
- review the annual audit plan and monitor the effectiveness of the external audit process;
- monitor and review the effectiveness of the outsourced internal audit function, including a review of the internal audit plan, all internal audit reports, and management's responses to the findings and recommendations of the internal audit function;
- consider the adequacy of the Group's finance function;
- review the Group's Tax Strategy; and
- review the Committee Terms of Reference.

The role of the Audit and Risk Committee is to oversee financial reporting. The Committee reviews the ongoing effectiveness of the Group's internal controls and provides assurance on the Group's risk management processes. The Committee also assesses information received from the external and internal audit functions.

Following the 2019 year end, at the March 2020 meeting, the Committee reviewed and recommended for approval by the Board, the financial results for the year ended 31 December 2019, including a review of the full-year external audit.

As part of that review process, the members of the Committee reviewed the Annual Report, including the adequacy of the disclosure with respect to going concern and viability reporting, in order to conclude whether the Annual Report taken as a whole was fair, balanced and understandable.

This additional review by the Audit and Risk Committee, supplemented by advice received from external advisers during the drafting process, assisted the Board in determining that the report was fair, balanced and understandable at the time that it was approved.

The Committee considered the appropriateness of preparing the accounts on a going concern basis, including consideration of forecast plans, and supporting assumptions, as well as sensitivity analysis and concluded that the Company's financial position was such that it continued to be appropriate for accounts to be prepared on a going concern basis.

Composition

The Audit and Risk Committee is chaired by Frank Nelson and comprises all three of the Non-executive Directors, but not the Chair of the Board, all of whom have served on the Committee throughout the whole year.

The Governance Code recommends that all members of the Audit and Risk Committee are Non-executive Directors, independent in character and judgement and free from any relationship or circumstance which may, could or would be likely to, or appear to, affect their judgement and that one such member has recent and relevant financial experience.

The Board considers that, by virtue of his extensive experience, details of which are set out on page 55, Frank Nelson, a Fellow of the Chartered Institute of Management Accountants, has recent and relevant financial experience and the Company complies with the requirements of the Governance Code in this respect. Furthermore, all Committee members have extensive relevant commercial and operational experience, particularly in building/construction organisations, which both benefit the Committee and collectively illustrate its competence relevant to the sector in which the Group operates.

Only members of the Committee have the right to attend Committee meetings, but both the internal and external auditors were invited to attend all meetings during the year, as a matter of course. Other individuals, such as the Chief Executive Officer, the Chief Financial Officer and other members of the Board were invited to attend the Committee meetings as and when appropriate. The Group Company Secretary also attends by invitation in order to maintain a record of the meetings.

In addition, the external auditor met regularly with the Committee without executive management being present and met separately with each of the Audit and Risk Committee Chair and the Chief Financial Officer.

The Audit and Risk Committee will meet as often as it deems necessary but, in accordance with its terms of reference, at least three times a year.

Summary of activities during the year

The Audit and Risk Committee met formally four times during the year and attendance at the meetings is shown on page 60.

The areas of particular focus for the Committee in 2019, and up to the date of this Annual Report, were as follows:

- Reviewed the 2018 and 2019 Annual Reports, as well as the 2019 Half-Year Report, including preliminary announcements.
- Considered information presented by management on significant accounting estimates and judgements adopted in respect of the Group's 2018 and 2019 Financial Statements and the 2019 Half-Year Report.
- Reviewed reports from the external auditor setting out their findings as a result of their audits for the years ended 31 December 2018 and 2019, as well as their review of the 2019 Half-Year Report.
- Reviewed the external auditor's plan for their audit for the year ended 31 December 2019.
- Reviewed documentation prepared to support the viability statement and going concern assumption set out on page 50.
- Considered the impact of new accounting standards and financial reporting requirements, including guidance issued by the Financial Reporting Council ('FRC').
- Considered reports by management related to the effectiveness of the Group's systems of risk management and internal control.
- Reviewed the Group's risk register, including principal and emerging risks.
- Considered reports prepared by the Group's outsourced internal audit function.
- Considered the results of the externally-facilitated assessment of the Committee's effectiveness.
- Approved updates to the Committee's Terms of Reference.
- Reviewed, and approved updates where applicable, to Group policies for anti-bribery, whistleblowing, capital expenditure and treasury, along with the Group tax strategy.
- Considered the impact of the revised ethic standard issued by the FRC in December 2019.

The Committee was also kept up to date with changes to accounting standards and developments in financial reporting, company law and other regulatory matters through presentations from the external auditor, Chief Financial Officer and the Company's Finance function.

Audit and Risk Committee Report **continued**

Key accounting estimates and judgements

As described above, the Committee reviewed the key estimates and judgements used in the preparation of the Group's 2019 Financial Statements (including a review of PwC's report and a discussion of their observations and findings in this area) as follows:

Area	Estimate/Judgement	Management's approach	Committee's review
Inventory valuation	Provisions for slow-moving items and discontinued product lines	Assessment of the appropriate level of provisioning against obsolescence, undertaken in the context of current trading and the forecast for the next financial year	Critically reviewed the carrying value of the Group's inventory, the approach taken by management and assessed the reasonableness of the underlying assumptions and financial forecasts used ¹ .
Accounts receivable recoverability	Provisions for bad and doubtful debts	Adoption of IFRS 9's expected credit loss approach to the impairment of receivables, which requires the use of forward-looking statistical modelling to determine the appropriate level of provision	Critically evaluated the methodology with respect to setting provisions for potential bad and doubtful debts, as well as the absolute level of provisions held ² .
Contract asset valuation	Carrying value/impairment of contract payments made to customers	Assessment of contract profitability and potential impairment, undertaken in the context of current and forecast trading levels	Considered the reasonableness of the key estimates and underlying assumptions and forecasts, as well the absolute asset value
IFRS 16 leases	Value of right-of-use asset and associated lease liability	Adoption of the modified retrospective approach to implementation, including the determination of lease terms (taking into account potential break clauses or lease-extensions) and the appropriate discount rate to be applied to future cashflows	Reviewed the methodology used and considered the reasonableness of the key estimates and underlying assumptions

Notes:

- 1 The Committee noted that there continues to be considerable management focus on both the optimisation of finished goods inventory levels and, looking forward, on the operational controls over the management of inventory.
- 2 The Committee's review also took into account the specific nature and characteristics of customers in the Group's 2 major divisions.

Risk management

The Group's risk management processes are set out in detail on pages 44 to 45.

The Group maintains a risk register that identifies key and emerging risks, the probability of those risks occurring and the impact they would have on the Group if unmitigated. Against each gross risk, the controls that exist to manage and, where possible, minimise or eliminate those risks are also listed, and an assessment of net risk is provided. The risk register also identifies any further actions required such that net residual risk is consistent with the risk appetite set by the Board. The register is regularly updated to reflect changes in circumstances.

The Group's Risk Management Committee is chaired by the Chief Financial Officer. This Committee reviews significant risks and the status of related mitigating actions each quarter.

The Audit and Risk Committee reviews the risk register twice per year to ensure the timely identification and robust management of inherent and emerging risks is taking place. To the extent that any failings or weaknesses are identified during the review process, appropriate measures are taken to remedy these.

Information relating to the management of risks and any changes to the assessment of key risks is reported by the Audit and Risk Committee to the Board.

Internal controls

The Board is responsible for the overall system of internal controls for the Group and for reviewing its effectiveness. In accordance with FRC guidance, it carries out such a review at least annually, covering all material controls including financial, operational and compliance controls and risk management systems.

In particular, the Board discharges its duties in this area by:

- holding regular Board meetings to consider the matters reserved for its consideration;
- receiving regular management reports which provide an assessment of key risks and controls;
- scheduling annual Board reviews of strategy including reviews of the material risks and uncertainties facing the business;
- ensuring there is a clear organisational structure with defined responsibilities and levels of authority which are regularly reviewed;
- ensuring there are documented policies and procedures in place; and
- scheduling regular Board reviews of financial budgets and forecasts with performance reported to the Board on a regular basis.

The Group has several operating policies and controls in place covering a range of issues including financial reporting, capital expenditure, business continuity and information technology, including cyber security, and appropriate employee policies. These policies are designed to ensure the accuracy and reliability of financial reporting and govern the preparation of financial statements.

In reviewing the effectiveness of the system of internal controls, the Audit and Risk Committee will continue to:

- review the risk register compiled and maintained by senior managers within the Group at least bi-annually and question and challenge where necessary;
- regularly review the systems of financial and accounting controls; and
- report to the Board on the risk and control culture within the Group.

In respect of the Group's financial reporting, the Finance Department is responsible for preparing the Group financial statements using a well-established process and ensuring that accounting policies are in accordance with International Financial Reporting Standards. All financial information published by the Group is subject to the approval of the Audit Committee.

There have been no changes in the Company's internal control during the financial year under review that have materially affected, or are reasonably likely to materially affect, the Company's control over financial reporting. The Board, with advice from the Audit and Risk Committee, is satisfied that an effective system of internal controls and risk management is in place which enables the Company to identify, evaluate and manage key and emerging risks and which accords with the guidance published by the FRC.

These processes have been in place since the start of the financial year and up to the date of approval of the accounts. Further details of specific material risks and uncertainties facing the business can be found on pages 46 to 49.

Internal audit

KPMG LLP provide an outsourced Internal Audit function which complements the internal finance-based checks performed on the branch network operations.

During 2019, the Committee worked with KPMG LLP to agree the programme for the year, which included reviews of the processes and controls relating to capital expenditure, procure-to-pay and cyber-security.

The Committee also formally reviews the Group's progress in implementing the improvement recommendations raised through the internal audit process in conjunction with the Executive Committee, who monitor a report on the status of the outstanding actions on a monthly basis. Both Committees found the progress during 2019 to be satisfactory.

External audit and auditors' independence

The Audit and Risk Committee has primary responsibility for making a recommendation to the Board on the appointment, reappointment, removal and remuneration of the external auditors. It keeps under review the scope and results of the audit, its cost-effectiveness and the independence and objectivity of the auditors.

The external auditor is required periodically to assess whether, in its professional opinion, it is independent and those views are shared with the Audit and Risk Committee. The Committee has authority to take independent advice as it deems appropriate in order to resolve issues on auditor independence. No such advice has been required to date. There are no contractual obligations in place that restrict the choice of statutory auditor.

The Group's current auditors, PwC LLP were appointed at the Audit and Risk Committee meeting on 29 April 2015, following the Company's IPO in March 2015. As a result, PwC LLP may remain as external auditor without re-tender for ten years from that date, until the completion of the 2025 annual audit. The Committee considers the need to tender the audit on an annual basis and there are no current plans to perform such a tender.

In accordance with best ethical standards, PwC LLP has processes in place designed to maintain independence, including the rotation of the audit engagement partner at least every five years. As a result of these processes, the current audit engagement partner will step-down following the 2019 audit and transitional arrangements are in place for his successor.

The Committee has also adopted policies to safeguard the independence of its external auditors. Any work awarded to the external auditors with a value of more than £5,000 in aggregate in any financial year, other than an audit, requires the specific approval of the Committee. Where the Committee perceives that the independence of the auditors could be compromised, the work will not be awarded to the auditors. Details of amounts paid to PwC LLP for audit and audit related assurance services in 2019 are set out on page 114. The audit related assurance services provided were in relation to the half-year report.

Prior to recommending the appointment of PwC LLP at the forthcoming AGM to the Board, the Committee reviewed the audit process, the performance of the auditor and its ongoing independence, taking into consideration input from management, responses to questions from the Committee and the audit findings reported to the Committee. Based on this review, the Committee concluded that the external audit process had been run efficiently and that PwC LLP has been effective in its role as external auditor.

The Committee is satisfied that the independence of the external auditor is not impaired and the level of fees paid for non-audit services, details of which are set out in Note 5 to the Financial Statements, does not jeopardise its independence. In conclusion, the Committee has assessed the performance and independence of the external auditor and recommended to the Board the re-appointment of PwC LLP as auditor until the AGM in 2021.

Whistleblowing and bribery

The Audit and Risk Committee monitors any reported incidents under our whistleblowing policy, which is available to all employees. This policy sets out the procedure for employees to raise legitimate concerns about any wrongdoing without fear of criticism, discrimination or reprisal. During the year, there was one report received through the whistleblowing process which was fully investigated and addressed in accordance with the policy.

The Audit and Risk Committee also takes responsibility for reviewing the policies and procedures adopted by the Group to prevent bribery. The Group is committed to a zero-tolerance position with regard to bribery. The Committee is satisfied that the Group's procedures with respect to these matters are adequate.