

#### 4. AUDIT COMMITTEE

- (a) Credit institutions shall have an audit committee. The audit committee shall be a stand-alone committee, shall be composed of non-executive directors, and shall have at least three members.
- (b) At least one member of the audit committee shall have competence in accounting and/or auditing:  
Provided that the chairperson of the audit committee shall have competence in accounting and/or auditing.
- (c) The members of the audit committee as a whole shall have competence relevant to the financial sector in which the audited credit institution is operating.
- (d) The members of the audit committee shall be appointed by the Board of Directors. The majority of the members of the audit committee shall be independent<sup>1</sup> of the audited credit institution.
- (e) The chairperson of the audit committee shall, subject to paragraph 4(b) above, be appointed by the members of the audit committee or by the Board of Directors and shall be independent of the audited credit institution.
- (f) Without prejudice to the responsibility of the members of the Board of Directors, the audit committee shall, *inter alia*:
  - i. inform the Board of Directors of the audited credit institution of the outcome of the statutory audit and explain how the statutory audit contributed to the integrity of financial reporting and what the role of the audit committee was in that process;
  - ii. monitor the financial reporting process and submit recommendations or proposals to ensure its integrity;
  - iii. monitor the effectiveness of the credit institution's internal quality control and risk management systems and, where applicable, its internal audit, regarding the financial reporting of the audited credit institution, without breaching its independence;
  - iv. approve and monitor the internal auditor's work programme, and receive internal audit reports or a periodic summary;

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<sup>1</sup> For the purposes of this paragraph, a director shall be considered to be independent only if such a director is a non-executive member who does not have any management responsibilities within the audited credit institution or within the Group to which that institution pertains. Furthermore, such a member of the Board of Directors should be free of any business, family, or other relationship ties including but not limited to, managerial responsibilities with such audited credit institution, its controlling shareholders or any member of the group of which the credit institution forms part, and is not under any other undue influence, internal or external, political or ownership, which would impede the board member's exercise of objective judgement.

- v. monitor the methods used by senior management to account for significant and unusual transactions where the accounting treatment may be open to different approaches, paying particular attention to both the existence of, and the justification for, any activity carried out by the credit institution in offshore centres and/or through special purpose vehicles;
- vi. monitor the responsiveness of senior management to the findings and recommendations of the internal audit function and make recommendations on the selection, appointment, reappointment and removal of the head of the internal audit department and on the department's budget;
- vii. monitor the statutory audit of the annual and consolidated financial statements, in particular, its performance, taking into account any findings and conclusions by the Accountancy Board established by the Accountancy Profession Act (Chapter 281 of the Laws of Malta), pursuant to Article 26(6) of Regulation (EU) No 537/2014;<sup>2</sup>
- viii. review and monitor the independence of the statutory auditors or the audit firms in accordance with Articles 22, 22a, 22b, 24a and 24b of Directive 2006/43/EC<sup>3</sup> and Article 6 of Regulation (EU) No 537/2014, and in particular the appropriateness of the provision of non-audit services to the audited entity in accordance with Article 5 of Regulation (EU) No 537/2014;
- ix. review the statutory auditor's or audit firm's compliance with applicable guidance relating to the rotation of audit partners, the level of fees paid by the credit institution, and other related regulatory requirements;
- x. review the effectiveness of the external audit process, and the responsiveness of senior management to the recommendations made in the statutory auditor's or audit firm's management letter;
- xi. monitor the statutory auditor's or audit firm's work programme and ensure it obtains timely information about any issues arising from the audit;
- xii. be responsible for the procedure for the selection of statutory auditor(s) or audit firm(s) and recommend the statutory auditor(s) or the audit firm(s) to be appointed in accordance with Article 16 of Regulation (EU) No 537/2014;
- xiii. investigate issues giving rise to any resignation of the statutory auditor or audit firm, and make recommendations as to any required action;
- xiv. act as the principal point of contact between the internal auditors, the statutory auditor or audit firm and the Board of Directors in order to ensure that in addition to having an effective working relationship with senior management, both internal and statutory auditors are guaranteed free access to the Board of Directors;

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<sup>2</sup> 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.

<sup>3</sup> 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, as amended by Directive 2008/30/EC of the European Parliament and of the Council of 11 March 2008 amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts, as regards the implementing powers conferred on the Commission; Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC; and Directive 2014/56/EU of the European Parliament and of the Council of 16 April 2014 amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts; and as may be further amended from time to time.

- xv. review the process whereby the credit institution complies with existing provisions regarding the possibility for employees to report alleged significant irregularities in the credit institution, by way of complaints or through anonymous submissions, normally to an independent director, and ensure that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action;
  - xvi. decide whether and, if so, when the Chief Executive Officer or Chairperson of the Board of Directors, the Chief Financial Officer (or senior employees responsible for finance, accounting, and treasury matters), the internal auditor and the statutory auditor or audit firm, should attend its meetings;
  - xvii. be entitled to meet with any relevant person outside the presence of executive and managing directors who do not form part of the Audit Committee, if it so wishes.
- (g) The audit committee shall present the yearly and, if applicable, half-yearly statements, to the Board of Directors for approval. The audit committee shall meet at least quarterly and shall report to the Board of Directors on its activities:
- i. at least quarterly in the case of credit institutions which are deemed to be significant in terms of Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions;
  - ii. at least bi-annually in the case of credit institutions which are deemed by the authority to be high-priority less significant institutions (“LSIs”) in accordance with the methodology of the Single Supervisory Mechanism (“SSM”)<sup>4</sup>; and at least annually for all other credit institutions not falling under points (i) and (ii).
- (h) In order to ensure the well-functioning of the audit committee, credit institutions shall, *inter alia*:
- i. ensure that the audit committee is not prohibited from obtaining advice and assistance from outside legal, accounting or other advisors as it deems

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<sup>4</sup> Article 97 of Regulation (EU) No 468/2014 of the European Central Bank of 16 April 2014 establishing the framework for cooperation within the Single Supervisory Mechanism between the European Central Bank and national competent authorities and with national designated authorities (SSM Framework Regulation), requires the ECB to “define general criteria, in particular taking into account the risk situation and potential impact on the domestic financial system of the less significant supervised entity concerned, to determine for which less significant supervised entities which information shall be notified.” In this regard, the ECB considers that an LSI can be deemed to be of “high priority” for various reasons. LSIs that are close to being classified as significant institutions due to their size are, de facto, considered “high priority”. Also, a minimum of three high-priority LSIs per country applies. Additionally, the intrinsic riskiness and the impact on the national economy are also taken into account in determining the high-priority LSIs. For the intrinsic riskiness dimension, the national competent authorities perform a risk assessment of the LSIs in the context of their ongoing supervisory activity and using the common SSM methodology. This assessment takes into account several elements, such as: the business model of the institution, its internal governance and risk management, its risks to capital, and its risks to liquidity and funding. The impact assessment of an LSI aims to evaluate its impact on the domestic financial system and on the SSM. For this purpose, it is not only the institution’s size (total assets) that is considered, but also its interconnectedness with the rest of the financial system. [Source: <<https://www.bankingsupervision.europa.eu/about/ssmexplained/html/hplsi.en.html>> last accessed on 01/8/2016]

necessary to carry out its duties, and provide the audit committee with appropriate funding to this effect;

- ii. provide an induction programme for new audit committee members, and subsequent relevant training on an ongoing and timely basis; and
  - iii. ensure that all audit committee members are provided with full information relating to the credit institution's specific accounting, financial and operational features.
- (i) In so far as the requirements relating to the audit committee are concerned, paragraphs 4(a) to 4(h) shall be read in conjunction with Regulation (EU) No 537/2014. Particular consideration should be given to Title III (Articles 16 to 19) of the said Regulation, relating to the appointment of statutory auditors or audit firms and to the transitional provisions set out in Article 41 of the same Regulation.
- (j) Notwithstanding the provisions pertaining to the requirements of the Audit Committee set out in the Listing Rules, paragraphs 4(a) to 4(i) shall also apply to credit institutions listed on a regulated market. In case of any conflict between the provisions of paragraphs 4(a) to 4(i) and the Listing Rules, pertaining to the requirements of the audit committee, a credit institution listed on a regulated market shall comply with the requirements set out in paragraphs 4(a) to 4(i).