Audit Committee Report

Mike McKeon
Committee Chair

"The Committee has championed the continued reinforcement of the Group's controls and compliance, positioning it well for a return to growth"

Primary role

To assist the Board in fulfilling its oversight responsibilities by reviewing and monitoring the integrity of published financial information, the adequacy and robustness of the system of internal control and management of risk and the adequacy and effectiveness of the internal audit function and external audit

The Committee's terms of reference, reviewed and approved annually, are available on the Company's website at www.nationalexpressgroup.com

Key responsibilities

- Monitor the integrity of the Group's published financial information and review and challenge as appropriate any significant financial judgements and estimates made by management
- Evaluate the adequacy, robustness and effectiveness of the Group's internal financial and other controls
- Support the Board in evaluating the adequacy, robustness and effectiveness of the Group's management of risk, in terms of identifying, managing and mitigating principal risks and identifying and mitigating where possible emerging risks
- Review the Group's policies, processes and controls for the detection and prevention of fraud, and for compliance with applicable laws, regulations and internal policies, including relating to anti-bribery, anti-slavery and data protection
- Approve the activities, review the findings and assess the effectiveness of the Company's internal audit function
- Monitor the activities, consider the opinions and assess the independence and effectiveness of the external auditor
- Review the Company's Annual Report and advise the Board whether, taken as a whole, it is fair, balanced and understandable, and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy

Activity highlights

- Reviewed and satisfied itself as to the integrity and fairness of the Group's half and full year financial statements and the appropriateness of their being prepared on a going concern basis
- Assessed and challenged the appropriateness of the Company's viability statement
- Assessed and challenged management's approach to key accounting judgements and estimates
- Reviewed the findings and monitored the effectiveness of the internal audit function, including changes in its composition and the evolution of its approach since its last external quality assessment
- Reviewed the opinions and monitored the independence and effectiveness of the external auditor, including changes in its working practices agreed as part of the audit tender
- Supported the Board in its management of risk by its continued programme of 'deep dive' reviews into divisional risk and its ongoing review of cyber risk
- Reviewed the framework of the Group's compliance programme and the corporate policies comprised within it
- Considered compliance with the terms of Covid-19 related grants and subsidies claimed during the year

Membership, meetings and attendance

Committee member	Appointed	Resigned	Meetings attended/ meetings held
Mike McKeon (Chair)[1]	03.07.15	–	5/5
Ana de Pro Gonzalo[1]	01.10.19	–	5/5
Carolyn Flowers[1,2]	04.12.21	–	0/5
Dr Ashley Steel[1,3]	01.01.16	03.12.21	5/5

*** The Committee thanks Dr Steel for her significant contribution to the Committee and welcomes Ms Flowers to the Committee**

1 Independent Non-Executive Director
2 Carolyn Flowers joined the Committee on 4 December 2021 but did not attend any meetings of the Committee in the year as none were held after the date she was appointed *
3 Dr Ashley Steel stood down from the Committee on 3 December 2021 when she stood down from the Board. She attended all the meetings of the Committee in the year as they were all held before the date she stood down *

Other attendees: Company Secretary and, by invitation, Company Chairman, Group Chief Executive Officer, Group Chief Financial Officer, Group Financial Controller, Group Head of Internal Audit, Group Legal Counsel, Group Head of Compliance & Risk and representatives of the external auditor, Deloitte LLP

Further information about the Committee members is set out on pages 52 to 54

Dear fellow shareholder

I am pleased to present the Audit Committee Report for 2021. During the year under review, the Audit Committee has ensured continued focus on and challenge of the going concern and viability assessments and management of risk as the Group began its recovery from the Covid-19 pandemic, and has championed the continued reinforcement of the Group's controls and compliance, positioning it well for a return to growth.

Financial reporting

The Committee is responsible for considering and satisfying itself, after consultation with the Company's external auditor, that the Company and its Group have adopted suitable accounting policies and appropriately applied the same, that management has made appropriate accounting judgements and estimates, that the adoption by the Company of the going concern basis of accounting is appropriate and that its viability statement is reasonable.

Key accounting matters

Details of the key accounting matters addressed by management when preparing the Consolidated Financial Statements, together with information about how the Committee assessed, challenged where appropriate and satisfied itself that the judgements and estimates made by management in relation to them were reasonable, are set out in Appendix 1 to this Report.

Going concern assessment

The Committee reviewed and robustly challenged management's assessment that the Group's financial statements for the six-month period ended 30 June 2021 and for the financial year ended 31 December 2021 should be prepared on a going concern basis.
Management developed both base case and reasonable worst case financial scenarios over a 12-month look forward period using assumptions about trading drawn from the Group's strategic plan, budget and latest financial projections. They then applied stress tests to both those scenarios to determine whether the Company would be able to meet its liabilities as they fell due, having regard to the Group's access to cash and other committed facilities and the covenant tests in such facilities, to which the Group has now secured further amendments through December 2022. The Committee satisfied itself that, in both the base case and reasonable worst case scenarios, the Group would have sufficient liquidity and be able to comply with its amended debt covenants and there was no more than a remote possibility that it would not be able to do so even after the application of the further stress tests. Accordingly, the Committee recommended to the Board that the Company's and its Group's financial statements at the half and full year be prepared on a going concern basis.

Viability assessment

The Committee also carefully considered management's view of the Company's viability for the three-year period ending 31 December 2024, including the rationale for assessing viability over a three-year period. The testing of viability involved the analysis of base case and reasonable worst case scenarios projected forwards over this three-year period by reference to trading assumptions drawn from the Group's strategic plan, and factored in the impact of risks including known and likely future climate risks that could materialise over this three-year period, offset by reasonable mitigations. The Committee satisfied itself that, in both the base case and reasonable worst case scenarios, the Group should be able to continue in operation and meet its liabilities as they fall due. Accordingly, the Committee recommended to the Board that the Company make its viability statement as set out on page 48 of the Strategic Report.

FRC review of 2020 accounts

The FRC conducts a review programme of FTSE 350 companies' annual reports and accounts. During 2021 the FRC conducted such a review of the Company's 2020 accounts and enquired into three specific areas of the Company's reporting.

The first sought clarification on whether any of the Group's Covid support grant or subsidy arrangements gave compensation for any of the Covid-related costs presented within separately disclosed items. Management responded that, correctly, they did not.

The second enquired why the Group recognised booking fees at the point of sale and treated them as consideration for a separate performance obligation to the corresponding ticket revenue. Although there is a separate legal obligation, management agreed prospectively to amend the Group's accounting policy to recognise booking fees in the period in which the related travel occurs as the amounts concerned are immaterial.

The third enquired about the Group's factoring of advance subsidy payments. The Group has a number of contracts with public bodies where the future cash flows are contracted. For some of these, where the cash flows are back ended, the Group enters into factoring arrangements with a bank to factor the future cash flows in advance of invoicing the customer, thus aligning better the cash inflows with the costs of operations. The amounts drawn down on such arrangements have historically been accounted for in a similar fashion to receivables factoring and the Group has, as for receivables factoring, clearly disclosed the amounts drawn down. Having regard to recent clarifications regarding the presentation of financial liabilities within trade payables, management proposed that it would be more appropriate for the resultant liability with the bank to be recorded within borrowings rather than trade payables as it does not relate to goods or services, nor does it represent amounts invoiced or formerly agreed with a supplier.

The Committee reviewed management's assessment of the accounting treatment of both booking fees and factoring of advance subsidy payments, including by seeking the view of the external auditor. While the Committee understood, and supported the rationale for, the accounting treatments previously adopted, on the basis of the new arguments presented it agreed with management's proposals to amend the accounting policies. The amendment to policy on booking fee recognition will be made prospectively and the amendment to the policy on factoring advance subsidy payments will take effect retrospectively and therefore the Balance Sheet and associated cash flows have been restated accordingly.

Following management's proposals and their review and acceptance by the Committee, the FRC has confirmed it has closed its enquiries.

Risk management

The Board has overall responsible for risk management. The Committee supports the Board by conducting 'deep dive' reviews into the Group's divisions' risk management activities as well as certain specific Group-wide risks, and by reviewing the Group's compliance programme.

Group risk appetite and principal and emerging risk review

The Board's risk appetite and assessment of the Group's principal and emerging risks, as well as a description of how the Group manages risk, are set out on pages 42 to 47 of the Strategic Report. The Group's climate-related risks and opportunities are considered in more detail in the TCFD disclosures on pages 35 to 39.

Audit Committee Report continued

Divisional risk reviews

During 2021, the Committee reviewed the Group's divisions' principal and emerging risks and their management of such risks. Additional dedicated meetings of the Committee were held at which risk and senior managers from each of the divisions presented their principal and emerging risk registers and explained how they were managing and where possible mitigating risk. Mirroring the Company's approved approach to Group-wide risk, the divisions record their risks in the form of heat maps which categorise both their likelihood and potential severity according to Group developed guidance. Each risk is then assigned a business owner who develops and oversees the delivery of mitigating actions, which actions are tracked at regular divisional management meetings.

The Committee observed that the Group's divisions had included both current and emerging strategic, financial, operational and reputational risks in their registers and had developed action plans to manage such risks over the different time profiles over which such risks could materialise. It was also pleased to note that certain matters identified as risks were also viewed as opportunities and that, following the exercise to identify climate-related risks and opportunities as described on pages 37 to 39, environmental risks had been identified and classified in all divisions' risk registers. Using insights gained from the Board's work on overseeing Group-wide risks and the Committee's work on reviewing divisional risks, the Committee was able to challenge each division on whether it had identified and appropriately classified its risks and whether it was adopting the most effective mitigation plans, and share best practices the Committee had observed within each division.

Through its reviews, the Committee has been assured that each of the divisions has a robust risk identification and management process and was pleased to see that risk management has become embedded in the day-to-day business activities and culture of the divisions. Such reviews also have served to deepen Committee members' understanding of the risks the Group's different businesses face and, through the Committee sharing this understanding with the wider Board, they have informed the Board's ability to appropriately set the Group's risk appetite, assess the Group's principal and emerging risks and weigh up risks with opportunities when taking key business decisions.

Cyber risk review

Cyber risk remained a standing item on the Committee's agenda in 2021, with the Group's ongoing cyber security programme, and the progress being made against the specific deliverables comprised in such programme, assessed at each of the regularly scheduled Committee meetings.

These assessments were made against the backdrop of a significant growth in the number of cyber attacks being experienced by companies generally. Indeed, the Company was subject to a specific cyber attack during 2021 but, thanks to the particular actions the Company had taken in 2020 under its cyber security programme, this attack was detected and neutralised without any loss of data or compromise to operational systems. However, it prompted management and, in turn, the Committee to review the aptness of the Group's cyber security programme. This review validated that such programme remained fit for purpose but that the timetable for certain deliverables under it should be accelerated, including the implementation of more standardised access controls across the Group's server estate and its internet facing software systems, and the roll-out of a new cyber security Group standard on cyber incident response, which were completed in the year.

Compliance risk

The Group has a range of existing policies and procedures for ensuring compliance with applicable laws and regulations and relevant codes of conduct, including Group-wide policies on business ethics, anti-bribery and corruption, modern slavery and whistleblowing, and divisional policies and procedures which either implement or supplement the Group policies having regard to local laws, regulations and best practice. The Group's whistleblowing procedures include access to an independently managed whistleblowing hotline via which the Group's stakeholders, including employees, can raise concerns, anonymously if they so wish. Reported concerns are duly investigated and acted upon by management or the functional support teams as appropriate, with serious cases and their outcomes reported to the Board.

Looking ahead to the reforms the UK Government is expected to make to audit practices and corporate governance following its consultation on restoring trust in audit and corporate governance, in 2021 the Group engaged a new dedicated Group Head of Compliance who has hands-on experience of developing and implementing compliance programmes in multi-national organisations. The Group Head of Compliance, working with the Group Chief Financial Officer and Group General Counsel and their teams, will keep the proposed reforms on audit and corporate governance under review and will lead the work and make recommendations to the Committee on how to comply with new legal requirements or implement new best practice recommendations.

Internal control

The Committee is responsible for monitoring the adequacy and effectiveness of the Company's system of internal control and reporting to the Board on the same.

System of internal control

The Company's system of internal control is based on a three lines of defence model, with a number of component controls operating at each of those lines, as illustrated in Appendix 2 to this Report.

Internal audit

The internal audit function acts as the third line of defence and provides the Committee with assurance on the effectiveness of the Company's first and second line internal controls, including financial controls and controls designed to prevent incidents of fraud. It does this through the independent observation and objective assessment of such controls via a programme of audits undertaken throughout the year against a plan reviewed and approved by the Committee.

During 2021, the Company enhanced its internal audit resources by engaging new team members in North America and by using more external resource in the UK, Spain and Morocco. The audit plan included: audits of standard divisional financial controls; audits of key safety and operational controls; audits of particular operational initiatives including the driver recruitment process in North America; and audits on core Group-wide controls and initiatives such as the delivery of the Group's cyber security programme and the effectiveness of the operation of the Group's whistleblowing procedures. In addition, in view of the growing importance of environmental reporting to investors, the internal audit team conducted an audit of the Group's controls around the collection and reporting of environmental data. Internal audit reported all the findings from its audits and recommendations for follow-up management actions to the Committee.

At the Committee's specific request, internal audit also conducted audits of the Group's claims for Covid-19 related subsidies and grants, which were supplemented by reviews by an independent accounting firm of certain aspects of such claims. The Committee was conscious of the reputational risk that could attach to making errors in such claims so assured itself that the Group's operating subsidiaries who submitted such claims were eligible to do so, had calculated their claims correctly and, where relevant, were complying with the conditions attached to the grants and subsidies.

Internal audit effectiveness

The Committee is responsible for monitoring the effectiveness of the internal audit function. In respect of its work in 2021, the Committee monitored this effectiveness by reviewing the scores colleagues, whose work or controls were subject to internal audit, awarded to the function on a 'value scorecard' and by making its own assessment of the quality of that work. The Committee is satisfied that the Company's internal audit function continues to be effective.

Significant weaknesses or control failures

Following its review of and conclusions from all elements of internal and external assurance, the Committee is satisfied that there are no significant weaknesses or control failures to report in respect of the Company's financial year ended 31 December 2021.

In respect of the Company's financial year ended 31 December 2020, the Committee reviewed the need to address some control findings in its North America finance function which were identified as a result of small manual calculation errors made in the 2020 financial close process. While these did not give rise to any material accounting errors in that year, management nonetheless instigated a review of the financial control environment in the North America division with the assistance of an independent accounting firm. This review identified that there was a generally good financial control environment and compliance culture in North America but that there were opportunities to formalise the operation or documentation of certain financial controls to mitigate ad hoc manual errors. The Committee considered these findings together with the recommended actions to address them and tracked the progress made by the North America finance function in implementing such actions during the year ended 31 December 2021. The Committee has satisfied itself that good progress has been made in improving financial controls in North America.

External audit

Deloitte LLP is the Company's auditor. Deloitte was first appointed as auditor in 2011 and, following its selection in the Company's audit tender conducted in 2020 and shareholders' approval given at the Company's 2021 AGM, was re-appointed in 2021. Deloitte's continued appointment will be subject to shareholders' annual approval at prospective Company AGMs. Jane Whitlock is the Company's new audit partner following the mandatory rotation of the Deloitte audit partner in 2021. The Company has therefore complied with the Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014.

External audit plan and fee

The 2021 external audit plan, which was prepared by Deloitte and reviewed and approved by the Committee, comprised full scope audit procedures for the Group's UK & Germany, ALSA (including enhanced procedures in Morocco) and North America divisions. It included: the review by Deloitte of the Consolidated Financial Statements; its challenge of management's significant judgements and estimates; its review of certain of the Group's key financial and fraud controls and of the risk of management override of controls; and its consideration of certain aspects of the Group's non-financial reporting, including the Group's TCFD disclosures. Deloitte's fee for undertaking the 2021 audit, of £2.0 million, proposed as part of its tender for re-appointment, was also approved by the Committee.

External audit effectiveness

The Committee is responsible for reviewing the effectiveness of the Company's external audit. The Committee did so by considering the outcome of colleagues' evaluation of the quality and efficiency of Deloitte's work and its own evaluation of that work. In addition, the Committee considered how Deloitte had performed against the tender commitments it made to the Company to develop and achieve more effective and efficient ways of workings with the Company. These included conducting earlier planning and ensuring prompt communications, using technology solutions to conduct aspects of the audit, and developing audit quality indicators. Having regard to the outcome of these evaluations and progress against its tender commitments, the Committee is satisfied that Deloitte performed its work to a high standard.

External auditor provision of non-audit services and independence

The Committee is also responsible for reviewing the auditor's independence and objectivity. The Company operates a non-audit services policy which sets out the permitted and prohibited non-audit services its auditor may be engaged to provide, for the purpose of safeguarding the auditor's objectivity. The Committee reviewed the policy during the year and determined it remained fit for purpose. It also reviewed the Company's compliance with the policy, which was confirmed as Deloitte performed only permitted non-audit services during 2021 for which its fees totalled £0.2 million, representing 10% of the total audit fee.

Having regard to the operation of the non-audit services policy during 2021, together with Deloitte's reports to the Committee confirming its independence at the half and full year and the rotation of the Deloitte audit partner in 2021, the Committee assured itself of Deloitte's ongoing independence.

Board assessment of effectiveness

Taking account of the Committee's work on assessing the effectiveness of the Company's system of internal control, and both the Committee's and its own work on assessing the Group's management of risk, the Board is satisfied that these are effective.

Fair, balanced and understandable

Having carefully reviewed the Company's 2021 Annual Report, and considered management's approach to its preparation, including in compliance with applicable laws and having regard to the UK Corporate Governance Code, the TCFD recommendations and the FRC's best practice guidance, and having heard the views of its auditor, the Committee recommended, and in turn the Board confirmed, that this report, taken as a whole, is fair, balanced and understandable, and provides the necessary information for shareholders to assess the Company's position and performance, business model and strategy.

Mike McKeon
Audit Committee Chair
9 March 2022

Audit Committee Report continued

Appendix 1 – Key accounting matters

The Committee considered the following key accounting matters as part of its review of the Consolidated Financial Statements:

	Key accounting matter	Committee action and conclusion
Impairment of goodwill (see note 14 to the Consolidated Financial Statements)	In determining whether assets are impaired, management is required to make a number of estimations and assumptions, including on future cash flow projections, discount rates and perpetual growth rates.	The Committee carefully considered management's work on the impairment analysis and testing of the value of the Group's goodwill balances, applying particular focus to the value of its ALSA division's goodwill in view of the lower level of headroom. These impairment assessments were based on modelled forecast cash flows, discounted using a country-specific weighted average cost of capital (WACC) and a terminal value based on a perpetual growth rate (PGR). Management refined its methodology for deriving the WACC during the year in order to bring it more in line with common practice, although this had limited impact on the resulting WACC. After considering the assumptions made by management in forecasting cash flows and its rationale for the WACC and PGR, and taking into account the auditor's views on these matters, the Committee concurred with management's view that goodwill is not impaired as at the balance sheet date.
Insurance and other claims provisions (see note 26 to the Consolidated Financial Statements)	The adequacy of the provisions associated with claims arising predominantly from traffic accidents and employee incidents in North America is subject to estimation based on an assessment of the expected settlement value of known claims together with an estimate of settlement values that could be made in respect of incidents that have occurred but not yet given rise to a claim at the balance sheet date. Given the level of uncertainty, complexity and judgement involved in making these estimations, there is a risk that the eventual outcome could be materially different from that estimated and provided for.	The Committee considered the information provided by management on the status of the North America and other material open claims made against members of the Group together with advice from external actuaries, legal counsel and insurance brokers, on the likely outcome of such claims, as well as management's explanation of the methodology used to determine the value of provisions for such claims. After challenging whether management had considered all material open claims and incidents that could give rise to claims and the external advice given in connection with them, the Committee concluded that management's estimation of the value of such claims was within an acceptable range of the potential outcomes and accordingly was fairly stated.
WeDriveU put option liability (see note 25 to the Consolidated Financial Statements)	The value of the liability of the put option over the shares in WeDriveU Holdings Inc. not already owned by the Group is subject to estimation of future earnings performance.	The Committee considered management's valuation of the put option liability. This took account of the fact that the option over 10% of the shares had been exercised during 2021, the option over a further 10% will be exercised during 2022, and the option over the remaining 20% shares is expected to be exercised in early 2023. The valuation also made assumptions about WeDriveU Inc.'s projected 2022 EBITDA performance and net debt position, together with the external auditor's views on that estimate. Following this review, the Committee concluded that management's valuation was reasonable.
Separately disclosed items (see note 5 to the Consolidated Financial Statements)	The Group presents profits and earnings per share measures before separately disclosed items to provide more meaningful information to shareholders on the Group's underlying performance. The classification of separately disclosed items requires management judgement having regard to the nature and intention of the transactions to which they relate.	The Committee considered the nature and extent of the separately disclosed items identified by management and its rationale for why they did not form part of the Group's Underlying Operating Profit (a key APM). The Committee noted that this was the second year that certain Covid-19 related incremental costs were separately disclosed, but satisfied itself that these represented either the re-assessment of estimations in respect of items recorded as separately disclosed items in the prior year, or that they represented the finalisation of activities such as restructuring programmes that commenced in 2020 and concluded in 2021. After discussion with management and the external auditor, the Committee concurred with the approach taken.
Onerous contract provisions (see note 26 to the Consolidated Financial Statements)	The Committee reviewed the approach taken by management in recognising £23.1 million as an onerous contract provision in respect of its RRX German rail concession.	The Committee reviewed management's assessment and concurred with the onerous contract provision recorded.
Pension liabilities (see note 34 to the Consolidated Financial Statements)	The determination of the defined benefit obligation of the UK defined benefit pension scheme depends on the selection of certain assumptions. In particular, a key area of estimation uncertainty is in respect of the discount rate.	The Committee reviewed the assumptions made by management in determining the defined benefit obligation, including considering the advice from independent qualified actuaries, and concluded that they were appropriate.

Appendix 2 – System of internal control

Third line of defence

Board of Directors
Sets and monitors delivery of Group strategy, sets Group risk appetite, assesses the Group's principal and emerging risks and approves significant matters reserved to it

Audit Committee
Assists the Board in assessing risk management and reviews the effectiveness of the internal audit function and the external audit

Internal Audit Function
Audits the effectiveness of the Company's first and second line internal controls through the independent observation and objective assessment of such controls

Second line of defence

Group Executive Committee
which monitors the frameworks, policies & procedures and effectiveness of the functions referred to below

Group Compliance Framework
under which corporate policies, such as those on anti-bribery and anti-slavery, are created and enforced

Group Whistleblowing Procedures
by which internal and external stakeholders can raise concerns about wrongdoing

Group Safety Policies
set minimum expectations for safety outcomes, such as speeding and driver risk monitoring

Group Standard Operating Procedures
set minimum standards for operations, such as vehicle maintenance and driver rostering

Group Risk Management Reporting Guidelines & Group Risk Director
which help track the management and, where possible, mitigation of risks and calibrate the severity and likelihood of risks

Group Cyber Security Programme & Group Cyber Security Team
which set cyber security strategy and control and monitor progress against that strategy and compliance with those controls

Group Environmental Data Reporting Guidelines & Group Sustainability Director
which help track delivery of environment strategy and ensure the integrity and consistency of environmental data collection and its reporting

Group Consolidated Financial Reporting & Group Finance Team
which consolidate and review Group financial results

Group Treasury & Tax Functions
which centrally manage Group treasury activities and set Group tax strategy and review tax compliance

Group Legal Reporting & Group General Counsel
which monitor, report and provide legal advice on Group legal risks

First line of defence

Divisional Executive Committees
which monitor the policies and procedures and the effectiveness of the functions referred to below

Divisional Safety, Operational, Cyber and Environmental policies and/or procedures
which implement Group policies and/or procedures

Divisional Risk Registers & Management
which track divisional risks and develop mitigations

Divisional Budgets & Forecasting
which set divisional financial expectations and monitor delivery

Divisional Finance Teams
maintain the financial ledgers and prepare divisional accounts

Divisional Legal Teams
provide legal advice and assistance on divisional legal risks