

# Audit Committee

**The Audit Committee (the 'Committee') is appointed by the Board from the Non-Executive Directors of the Company. The Chair of the Committee is Chris Morgan.**

## Audit Committee composition and meetings

Chris Morgan's previous roles have given him senior executive and financial experience working across a number of technology and digital printing sectors and across a number of jurisdictions. Alison Littlely, Audit Committee member, also brings a breadth of experience including executive experience in complex, international business operations. Additional information on our skills and experience can be found in the Board biographies set out on pages 60 and 61.

The Audit Committee met formally on seven occasions during the year and details of the attendance at meetings by members of the Audit Committee are set out on page 76. Please see the tables on page 76 for details of the Committee members in the year and the number of Committee meetings attended. At the Committee's request, other members of the Board and senior management may be invited to attend the Audit Committee's meetings based on the meeting agenda.

## Report from the Committee Chairman

I am pleased to present the Audit Committee's report describing our work during the past year. Ernst & Young LLP (EY) was reappointed as the Group external auditor at the Annual General Meeting and Adrian Bennett is the engagement partner.

The Audit Committee's primary responsibilities are the following:

- To approve and monitor key financial and accounting policies and practices
- To monitor the integrity of the financial statements, announcements and review significant financial reporting judgements contained therein
- To keep under review the adequacy and effectiveness of internal controls
- To review procedures, systems and controls for whistleblowing, fraud detection and bribery prevention
- To review, approve and monitor internal audit activities
- To monitor and review the Group's external auditor's independence, objectivity and effectiveness
- To monitor and approve any non-audit services provided by the external auditor
- To conduct any tender process and make recommendation to the Board on the appointment, remuneration and terms of engagement of the external auditor.

The Committee is not responsible for the identification of key risks or the review of the adequacy of arrangements to mitigate those risks, which remains the responsibility of the Board.

The Committee is required to report its findings to the Board at least annually, identifying any matters on which it considers that action or improvement is needed, to make recommendations on the steps to be taken, and to ensure that the required actions are implemented. The Committee shall review its terms of reference annually and may recommend to the Board any amendments. The Committee's terms of reference include all matters indicated by Disclosure and Transparency Rule 7.1 and the 2018 UK Corporate Governance Code. The terms of reference of the Committee are available on written request from the Company Secretary.

## Significant issues considered by the Committee

The Committee has a work plan that is designed to ensure its responsibilities are fully discharged over the annual reporting cycle. Specific items are added to the agenda for individual meetings as required. There were a number of significant accounting matters considered during the year including:

- Revenue recognition
- Valuation of Xaar 3D disposal contingent consideration
- FFEI acquisition
- Impairment of goodwill, intangible assets and PPE
- Inventory valuation and obsolescence, including EPS' H1 2021 non-cash adjustments relating to slow moving and obsolete inventory
- Consideration and treatment as a prior year adjustment of the remediation of the significant deficiencies in internal control identified within EPS as part of the 2020 year end audit process, as described on page 79.

## Key areas of management judgement

The Committee has reviewed, discussed with and challenged management in respect of the approaches taken for the following areas of key accounting judgement and estimation:

### Accounting judgements

#### Capitalisation of development costs – note 16

The Audit Committee considers management's assessments when the criteria for capitalisation are met. The development of the High Speed Sintering in 3D was completed in December 2020, the cost and accumulated depreciation was reclassified as part of an asset group held for sale as at 31 December 2020, and subsequently disposed of in 2021.

#### Discontinued operations – note 11

The 3D business met the criteria of a discontinued operation in December 2020 and the disposal was formally completed on 1 November 2021. The accounting treatment of the disposal of the Xaar 3D business reclassified as discontinued operations has been presented to, considered and agreed by the Audit Committee and the external auditors.

### Estimation uncertainty

#### Climate-related risks – Risk management

Climate change is a global challenge and an emerging risk to businesses, people and the environment across the world. In management's view and the Audit Committee's review, climate change does not currently create any further key sources of estimation uncertainty for the Group.

#### Contingent consideration – note 22

The contingent consideration is a financial asset measured at fair value, which is calculated using the Monte Carlo Simulation model, the model uses a number of inputs that require estimation: forecast revenues, time until expiration, expected volatility and discount rates. Third party experts are used to provide these inputs, but the estimates remain uncertain. The valuations are considered by the Audit Committee on review of the accounting treatment of the disposal of the Xaar 3D business.

#### Inventory provision – note 20

A policy is used by management to calculate the inventory provisions based upon use and ageing of inventory; a significant proportion of the inventory provision relates to discontinued operations.

#### Credit provision for the allowance of doubtful debts – note 21

A review has been undertaken to consider the requirements of IFRS 9 and the expected credit loss provision requirements based on historical default and loss experience by management.

#### Impairment of capitalised development costs – note 16

The Group determines whether capitalised development costs, and all other non-current assets, are impaired at least on an annual basis. The carrying amount of capitalised development costs at 31 December 2021 was £nil.

#### Impairment of goodwill in relation to EPS – note 15

The Group tests goodwill annually for impairment. A budget has been prepared for EPS and a cash flow forecast derived to determine a value in use calculation. The recoverable amount is estimated and discounted with regards to a discount rate applicable to EPS, this reflects external third party advice and input estimates of the risk free rate, equity beta and market premium calculated at the year end. Sensitivity analysis is undertaken, but the estimates remain uncertain and rely upon forward guidance. Management's assessment has been reviewed by the Audit Committee, which is satisfied that there is no impairment identified.

#### Revenue recognition – note 5

The Audit Committee reviews the assessment of the application of IFRS 15, as presented to it, with regards to the stage of completion for relevant customer contracts.

 **Additional disclosure in relation to key sources of estimation uncertainty and critical accounting judgements is provided in the Group financial statements – note 2 on pages 119 and 120**

### Key activities

In discharging its responsibilities, the Committee has completed the following activities:

#### Financial statements and reports

- Reviewed the Annual Report, financial statements and the half-yearly financial report including disclosures made therein, and confirms that taken as a whole, they are fair, balanced and understandable, and provide the information necessary for shareholders to assess the position, performance, strategy, and business model of the Company
- Reviewed Going Concern and Viability Statements and supporting assessments
- Reviewed reports from the external auditor on their work and findings
- Reviewed the effectiveness of the Group's internal control environment.

## Internal controls and compliance

To assist the Board with its responsibilities to effectively determine the nature and extent of the Group's significant risks (as described on pages 44 and 45), the Committee carries out a robust annual assessment of the principal risks and uncertainties facing the Group. The Board remains ultimately responsible for determining the nature and extent of the effectiveness of the risk management and internal controls systems which mitigate potential impacts on shareholder investments and the Company's assets. The Corporate Risk Register is reviewed and challenged bi-annually by the Audit Committee.

The Committee having performed the annual review of the Group's internal control processes considers the systems to be effective and in accordance with the Guidance on Risk Management, Internal Control and Related Financial and Business Reporting as issued by the FRC. In order to support the growth of the business and the implementation of Company strategies, the Committee recognises the need to continue to review the adequacy and effectiveness of our control framework.

The Committee undertakes this evaluation having:

- Reviewed the internal financial controls and risk management systems
- Reviewed fraud detection and the systems and controls for the prevention of bribery including employee confirmation of abiding by the Code of Conduct, Anti-bribery & Corruption, and Whistleblowing policies
- Reviewed and approved actions for improvements to Treasury management
- The Committee considered and reviewed the internal audit plan that in 2020 was unable to progress as planned due to the impact of COVID-19 restricting the ability to travel to overseas sites alongside requirements to work from home, which continued to disrupt plans in 2021. A review was undertaken for the approach of internal audit, internal resource was recruited (joined in January 2022) and an external provider was engaged to commence internal audit activities in 2022. In addition, an audit readiness engagement was performed at EPS in the place of an internal audit in 2021 (see more detail below).

In line with the provisions of the UK Corporate Governance Code 2018, the Committee monitors and reviews the effectiveness of the Company's internal audit function or, where there is not one during a period, considers annually whether there is a need for one. The Committee recognises the challenges faced over the last two years, and has ensured steps have been taken to commence internal audits of financial processes and controls in 2022 across the Group. The Committee sanctioned an approach for greater emphasis to be placed on the methodology and effectiveness of management controls. This was implemented during 2021 with the objective to identify effective and ineffective processes and controls, and will drive increased engagement with internal audit in the future through the design and implementation of new internal systems to ensure a robust and effective solution.

As disclosed in the Xaar plc Annual Report and Financial Statements 2020, significant deficiencies in internal control were identified in the EPS subsidiary during the external audit process for the year ended 31 December 2020, in respect to the financial statement close process and management controls. An action plan was established, presented to the Board and Audit Committee, and implemented in 2021, covering the actions required to remediate the internal management and reporting controls and remediate the identified deficiencies. The significant deficiencies in internal control identified in the EPS subsidiary were in respect of the adequacy of controls in the financial reporting close process, controls over revenue recognition, and controls over inventory management and valuation.

The action plan was substantially underway by the end of 2021, enabling the delivery of improved operational processes across the business and addressing the concerns raised during the external audit of the 2020 financial year. The Board and the Audit Committee are kept up to date with the progress made against the action plan. A third party, RSM LLP US (RSM), were engaged to support the audit readiness of EPS ahead of the 2021 year end audit. In addition to reviewing actions taken during 2021, RSM helped to identify and implement further actions as required to enable a successful year-end external audit. This engagement was undertaken ahead of traditional internal audit activities in order to provide assurance that appropriate processes have been performed resulting in accurate accounting, free from significant deficiencies in internal controls.

Further to this, RSM will work with EPS in relation to risk and controls to ensure we have clear integrated controls and reporting across the EPS business. This work will be enhanced further by internal audit procedures to follow later in 2022 once clear processes and controls have been established at EPS. Work continues across the business to enable delivery of improved operational processes, however the actions taken to date have resulted in significant progress being made, with clear and demonstrable improvement in operations, process and culture.

The Committee remains of the view that the statement made regarding the Company's viability period continues to be an accurate assessment of the Company's viability as at the date of the report. The Viability Statement can be found in full on page 68.

## FRC's Corporate Reporting Review

Xaar plc's Annual Report and Accounts to 31 December 2020 was selected as part of the FRC thematic review of companies' disclosure of alternative performance measures (APMs); as such, only the disclosures in relation to APMs were reviewed. Xaar's disclosure relating to the cash flow impact and tax effect of restructuring costs was highlighted as an example of better practice in the FRC Thematic Review: Alternative Performance Measures (APMs), published in October 2021. A request for information was also made; Xaar provided a response covering the specific questions raised and on 10 November the FRC confirmed that the matter was brought to a satisfactory conclusion. The FRC asked Xaar to explain the difference between the amount of depreciation of property, plant and equipment disclosed within the reconciliation of adjusted EBITDA, and the depreciation charge disclosed elsewhere in the notes to the accounts. We provided a satisfactory analysis and clarified that the main difference related to an impairment charge. We also stated that the depreciation of right-of-use assets was not added back when arriving at the adjusted EBITDA. We confirmed that the nature of the reconciling items, and the reasons for their selection, would be clarified in the next Annual Report and Financial Statements.

## Audit Committee continued

Note that there are inherent limitations in the FRC's review as the FRC provides no assurance that Xaar's 2020 Annual Report and Financial Statements are correct in all material aspects; their role is not to verify the information provided but to consider compliance with reporting requirements. The FRC accepts no liability for reliance on them by Xaar or any third party, including but not limited to investors and shareholders.

### External audit

- Following the conclusion and sharing of the 2020 audit results, there was an extensive collaborative effort by the Xaar and the EY teams to review the process in detail, and identify and implement improvements for future audit efforts including improved planning and timing of audit procedures, as well as working team adjustments to better handle engagement given the dynamic COVID-19 situation. This process work and the related recommendations were reviewed by the Audit Committee and were instrumental in aiding the planning of the 2021 audit
- The Audit Committee provided a forum for reporting and discussion with the Group's external auditors in respect of the Group's full-year results. The Committee had dedicated time for these activities and reviewed the audit work with emphasis on significant risk areas identified and discussed by the external auditor in their report
- The scope of the audit work to be undertaken by the auditor was reviewed and agreed on
- The Committee agreed the fees to be paid to the external auditor relating to their services rendered for the annual audit
- The independence and objectivity of the external auditor was assessed by the Committee.

The Chairman of the Audit Committee will be available at the AGM to answer any questions about the work of the Committee.

### External auditor

This was the third year for Ernst & Young LLP (EY) as the Company's auditor having first been appointed in July 2019 after a competitive tender. For the second year the senior statutory auditor is Adrian Bennett. The Committee has met with the auditor on at least three occasions during the year and it is expected that the Committee will continue to meet with the auditor a minimum of two times each year. The Chief Executive Officer and Chief Financial Officer, and other relevant managers and Board members, may attend these sessions by invitation, except for a period of each meeting where the Committee members may meet with the auditor without any member of executive management present.

The Committee is required to assess the qualifications, expertise, resources, and independence of the external auditor, and the objectivity and effectiveness of the audit process. The Committee reviews the type of work, effectiveness of, and level of fees charged by the auditor on an annual basis and recommends to the Board the appointment, reappointment, term, remuneration, and terms of engagement of the external auditor.

The Committee safeguards auditor objectivity and independence through maintaining a dialogue with the auditor and by monitoring all fees paid. It is the policy of the Group not to engage the statutory auditor in any non-audit related services. This includes tax services. Specifically, the policy states that the preparation of tax forms, payroll tax, calculation of indirect tax and the provision of tax advice cannot be provided by the statutory auditor. EY were engaged to provide tax services for FFEI for their year ending 31 March 2021, however on the completion of Xaar's acquisition of FFEI, there was no open work and EY discontinued their engagement as tax advisor.

Note 8 to the consolidated financial statements includes disclosure of the auditor's remuneration for the year.

The Committee, taking into consideration relevant UK professional and regulatory requirements, regularly considers the independence and objectivity of the auditor. The Committee receives an annual statement from the auditor detailing their independence policies and safeguards, and confirming their independence, taking into account relevant ethical guidance regarding the provision of non-audit services by the external auditor.

The Committee considers the effectiveness of the external audit and the Group's relationship with the external auditor on an ongoing basis. In completing the review of the effectiveness of the annual audit in 2021, the Committee was able to conclude the audit undertaken by Ernst & Young LLP was effective. This review consisted of considering a number of key points together with the senior financial management of the Group. A similar exercise will be undertaken following completion of audit procedures on the 2021 results and reported on in next year's Annual Report.

### Review of the Audit Committee's effectiveness

The Committee has reviewed and considered the effectiveness of its performance during the year. The review included the views of members of the Committee and of regular attendees at the various meetings (including the Executive Directors).

I am satisfied that the degree of rigour and challenge applied in performing the Committee's responsibilities is appropriate and effective.



**Chris Morgan**

Chair of the Audit Committee