

AUDIT COMMITTEE REPORT

**Michael Shallow**

Chairman of the Audit Committee

Dear shareholder

I am pleased to introduce the report of the Audit Committee for the 52 weeks ended 30 June 2018.

The Code recommends that all members of the Committee be 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 at least one such member has recent and relevant financial experience. Accordingly, the Committee comprises all three independent Non-executive Directors with me as Committee Chairman, considered by the Board to have recent and relevant financial experience due to my previous experience in senior financial roles. For the period between 17 October 2017 and 24 June 2018, Keith Edelman served as Executive Chairman during which period he continued to be a member of the Committee and, therefore the Company was not in compliance with the Code during this period. Given that the Committee comprises only three members and that the majority were independent Non-executive Directors during this period and given the issues under review by the Committee during this period, I as Committee Chairman was satisfied that this was in the best interests of the Company and its shareholders.

I have previously held senior finance positions in large leisure sector companies including finance director of Greene King plc and have been a non-executive director and audit committee chairman at Britvic plc, Spice plc (now EnServe Group Limited) and Domino's Pizza Group plc.

I am, therefore, suitably experienced to perform the role of Audit Committee Chairman and have a good understanding of the sector in which the Group operates.

Regular Committee meetings are also normally attended by the Chief Financial Officer and the external auditor. The Chief Financial Officer, who is also the Company Secretary, acts as secretary to the Committee. Other members of management, particularly senior financial managers, are invited to attend depending on the matters under discussion.

The Committee meets at least twice a year at the appropriate times in the reporting and audit cycle and also at least twice per annum ensures that there is meeting time with the external auditor with no members of management present. The Committee was set up by the Board to assist it with its responsibilities in respect of financial reporting, including reviewing annual and half-year results, external auditing, internal controls, and advising on the independence and appointment of the external auditor. The Committee also routinely examines significant accounting treatments facing the Group and will focus on those matters raised by the external auditor which they consider to be of significant audit risk.

Following completion of the Group's audit for the 52 weeks ended 30 June 2017 and the other associated formalities, the Committee reflected on the difficulties that the Group had experienced on its financial reporting (as reported in last year's Committee report) which had given rise to a significant number of prior year adjustments. The Committee decided that a change of auditor was appropriate and accordingly a tender process was

undertaken by the Committee resulting in the resignation of KPMG LLP and appointment of PricewaterhouseCoopers LLP ("PwC") as the Group's external auditor on 29 January 2018. The Committee is satisfied that, since the date of appointment, PwC has undertaken its responsibilities as the Group's external auditor to a high standard and therefore the Committee will be recommending that PwC be formally appointed as auditor at the 2018 annual general meeting ("AGM"). The PwC audit partner responsible for the Group is Randal Casson.

During the year, the Directors continued to assess the following key areas:

- > Board governance, including the Committee and the procedure for assessing the Group's key risks;
- > management accounting processes and the quality of information provided to the Board;
- > external financial reporting procedures and audit arrangements and reporting standards;
- > complex transactions, potential exposure and risk;
- > information systems; and
- > budgeting and forecasting procedures and controls.

The Directors recognise the need to maintain the financial reporting procedures, review them on a continuing basis and adapt them to changing circumstances. Their review forms part of the Committee's agenda going forward together with its wider role and responsibilities, which are set out in more detail in this report.

I look forward to meeting with shareholders at the AGM to answer any questions on the work of the Audit Committee.

Assessing effectiveness of external audit process

Whilst the Committee does not rely solely on the work of the external auditor, it regards the breadth and quality of the work performed by the external auditor as contributing significantly to several of the Committee's objectives, particularly regarding assurance relating to the accuracy and reliability of its external reporting and for reviewing objectively the Group's systems and internal controls. For that reason, planning meetings are held with the external auditor to review its proposed work programmes and any recommendations made by the external auditor is reviewed in depth as are its findings from its review of the half-year and year-end accounts. The Committee meets to discuss the performance of the external auditor and to consider priorities for future work. This review process led to the decision to change the external auditor earlier in the year.

In order for the auditor to be fully effective, it must be independent of the Company and the Committee intends to ensure that no other work is performed by the external auditor so that its independence is not compromised. New EU legislation on permitted non-audit services came into effect from 17 June 2016 which introduced a permitted non-audit services fee cap of 70 per cent of the average audit fee over a consecutive three-year period. This cap comes into effect for the Group in the financial year ending 30 June 2020. During the year the value of non-audit

services provided by the external auditor amounted to 0.15 million (2017: £0.02 million). The non-audit services relate to work performed by PwC prior to its appointment as external auditor. This non-audit work was referred to in last year's Audit Committee Report and related to an investigation into and a report to the Committee on the Group's accounting for supplier rebates and short-life assets. This work was substantially completed prior to the completion of KPMG LLP's audit of the results for the 52 weeks ended 30 June 2017 and subsequently a related smaller piece of work was undertaken by PwC to finalise the investigation. This work was completed before PwC was invited to participate in the tender process for the appointment as the Group's external auditor and both the Committee and PwC carefully considered whether there was any conflict of interest and were satisfied that there was not. The Committee does not intend that PwC will be engaged to perform any other non-audit services other than to review the Group's interim reporting, which it considers to be both incidental to the role as auditor and helpful to performing its role as auditor.

Under the EU audit regulation, the Company is required to undertake a tender for audit services at least every ten years (being for the period commencing July 2024). In light of the appointment of PwC as external auditor during the year, there are no plans to undertake a tender in the foreseeable future.

Role and responsibilities

The Committee's terms of reference can be found on the Group's website or alternatively can be obtained from the Company Secretary. The primary function

of the Audit Committee is to assist the Board in fulfilling its responsibilities to protect the interests of shareholders with regard to the integrity of financial reporting, audit, risk management and internal controls. This comprises:

- > monitoring and reviewing the Group's accounting policies, practices and significant accounting judgements;
- > receiving the annual and half-yearly financial statements and any public financial announcements and advising the Board on whether the annual report and accounts is fair, balanced and understandable in relation to the external audit;
- > reviewing compliance with the UK Corporate Governance Code;
- > overseeing the Group's procedures for its employees to raise concerns through its whistleblowing policy as set out in the code of conduct and business principles policy;
- > monitoring the effectiveness of the risk management systems and processes;
- > assessing and advising the Board on the internal financial, operational and compliance controls; and
- > approving the appointment and recommending the re-appointment of the external auditor;
 - > its terms of engagement and fees;
 - > the scope of its work and reviewing the results of that work;
 - > reviewing and monitoring its independence; and
 - > reviewing its effectiveness.

Meetings and attendance

During the 52 weeks ended 30 June 2018, the Audit Committee met formally on five occasions, with all members attending the meetings. At two of the meetings, the Audit Committee had access to the external auditor without management present.

Work performed by the Committee during the year has included:

- > engaging PwC to undertake a review of the Group's historical accounting for supplier rebates and short life assets and receiving and reviewing PwC's interim findings and commissioning a related smaller piece of work to satisfy further the Committee's further questions in relation to these matters;
- > work associated with the accounting review and application of accounting policies;
- > resignation of KPMG LLP and undertaking a tender for audit services culminating in the appointment of PwC as the Group's auditor;
- > reviewing the independence and objectivity of PwC as external auditor, together with its effectiveness, following its initial audit and recommending its appointment to shareholders at the AGM;
- > receiving the external auditor's reports to the Committee in respect of the interim audit review;
- > reviewing and approving the external audit plan for the 52 weeks ended 30 June 2018;
- > reviewing the market update in June 2018;
- > reviewing the annual report and accounts for 2018 and recommending to the Board its adoption as fair, balanced and understandable. In fulfilling this task, the Committee reviewed the process undertaken to produce the annual report and accounts 2018, which included internal verification processes and content approval procedures;

- > receiving the external auditor's reports to the Committee;
- > reviewing the Group's accounting policies and key accounting judgements;
- > considering the risk assessment, mitigation actions and assurance activities produced by management; and
- > reviewing compliance with and explaining any exceptions from the UK Corporate Governance Code.

Internal audit

The Group does not have an internal audit function and to date has considered that the key risks to the business are covered by a combination of resources including its compliance department, stock-takers and area managers.

The Group's compliance department is responsible for managing many of the principal risks facing the business concerning licensing and health and safety. Its work is supported by external consultants on both of these matters and as part of these arrangements annual contracts are in place to provide at least two audit visits per annum by fully qualified health and safety advisers.

To strengthen and complement this function a Risk Committee has been established chaired by the Chief Financial Officer and comprising certain members of the Senior Management team. The purpose of the Committee is:

- > to identify, mitigate and prevent risk as far as possible;
- > to protect the financial, physical and reputational image of the business;
- > to fulfil the Company's legal obligations; and
- > to ensure visibility and transparency over controls.

The Committee's terms of reference are available from the Company Secretary and can be found on the Company's website at www.revolutionbarsgroup.com.

During the period the Committee met formally on two occasions with all members attending. The key activities of the Committee during the period have been:

- > to ensure any critical issues arising from the audits carried out by the external consultants are rectified in a timely function;
- > to monitor health and safety issues in venues including certification compliance, review of risk assessments, food safety issues and review of insurance matters;
- > to ensure the Company adheres to the licensing objectives to protect all premises licences; and
- > to advise on changes in relevant legislation and policies.

The Group also employs four full-time stock-takers who are checking stocks and various other generally related compliance matters such as cash counts on a risk-assessed basis. Each site's stock is counted on average between eight and ten times per annum. Stock-take results are reviewed by both operational and finance staff immediately when they are made available.

An important element of the area manager's role is to perform spot checks on cash, stocks, licensing and health and safety matters as part of their regular site visits. The area manager assessments are used, amongst other things, to rate general managers; poor scores relating to these matters and brand standards will reduce their bonus earnings potential.

Significant accounting matters

During the year, the Company received a "Request for information" from the Financial Reporting Council, in respect of certain matters, principally deferred taxation credits and share-based payment disclosure, in the Group's annual report and accounts to 1 July 2017. As a result of the subsequent internal review, the Group has restated its Financial Statements in respect of a deferred taxation credit. The full nature of this restatement is reported in Note 1b to the Financial Statements. The Group has also improved its share-based payment disclosures, as reported in Note 19 to the Financial Statements. The FRC enquiry in respect of these matters was closed on 26 July 2018.

When reviewing the Company's 2017 Annual Report and Accounts, the FRC has made clear to us the limitations of its review as follows:

- > its review is based on the 2017 Annual Report and Accounts only and does not benefit from a detailed knowledge of the Group's business or an understanding of the underlying transactions entered into;
- > communications from the FRC provide no assurance that the Company's 2017 Annual Report and Accounts are correct in all material respects and are made on the basis that the FRC (and its officers, employees and agents) accepts no liability for reliance on them by the Company or any third party, including but not limited to investors and shareholders; and
- > the FRC's role is not to verify information provided but to consider compliance with reporting requirements.

In reviewing the financial statements with management and the external auditor, the Committee has discussed and debated

the critical accounting judgements and key sources of estimation uncertainty as set out in Note 1 to the consolidated financial statements.

As a result of its review, the Committee has identified the following issues that require particular judgement or have significant impact on the interpretation of the Annual Report and Accounts for 2018:

- > **Accrued rebates from suppliers:** rebates are usually invoiced on a monthly or quarterly basis based on supplied volumes and whilst these can usually be quickly assessed post-period, judgements are also sometimes required as to whether longer-term contractual thresholds will be met. Due to improved controls implemented during the year and regular monthly reviews undertaken by senior finance management, the requirement for judgements to be applied has been reduced dramatically. Where relevant, the Committee is satisfied that appropriate judgements have been made.
- > **Carrying value of fixed assets:** the Group keeps the carrying value of its fixed assets under review. Formal procedures are used in each external reporting period to make assessments of the appropriateness of carrying values within the balance sheet. As a result of its reviews, the Committee has applied accelerated depreciation rates on certain leasehold improvements.
- > **Capitalisation of property, plant and equipment:** the Committee has reviewed capitalisation policies and in particular the capitalisation of internal costs in relation to property development and IT systems development and is satisfied that its policies and the amounts capitalised are appropriate.

- > **Accounting for and the disclosure of a prior period adjustment in respect of impairment calculations:** The Committee became aware during the period that impairment calculations undertaken previously had not fully allocated head office costs to sites and this error of principle resulted in certain sites becoming impaired. The Committee was consulted and reviewed these calculations.
- > **Exceptional items:** exceptional items on a pre-tax basis of £11.1 million (2017: £2.3 million) represent a material item in the profit and loss account. The charge comprises fees associated with the resignations of the Chief Executive Officer and the Chief Operating Officer, fees associated with the accounting review, professional fees associated with the unsolicited approaches to the Company from Stonegate Pub Company Limited and the Deltic Group, which culminated in a formal offer being put to a shareholder resolution at an extraordinary general meeting, an increase in the provision for onerous leases, and a fixed assets impairment charge (see Note 3 to the consolidated financial statements). The Committee reviewed the constituent elements of this cost and was satisfied that they were exceptional in nature.

The Committee reviewed reports presented by PwC that detailed key audit findings in relation to the above accounting matters.

Michael Shallow

Chairman of the Audit Committee
2 October 2018