Report of the Audit Committee

Members: Alison Reed (Chairman), Maarten van den Bergh, Baroness Kingsmill, Ken Smart and Baroness Symons.

The Board is satisfied that Alison Reed has recent and relevant financial experience for the purposes of paragraph C.3.1 of the Combined Code.

The Committee met five times during the year ended 31 March 2010.

Regular attendees at Committee meetings, at the invitation of the Committee, included the Chairman, the Chief Executive, Chief Financial Officer, the Head of Corporate Risk and Internal Control, the Group Financial Controller, the Group Reporting Manager and representatives from the external auditor. Other senior management are invited to attend when the business of the Committee requires, in particular areas such as Information Technology. During the course of the year, the Committee has also held closed meetings and has also met privately with both the external and internal auditors.

The Audit Committee is responsible for exercising the full powers and authority of the Board in accounting and financial reporting matters. The full terms of reference are available on the Company’s investor relations website, bashares.com.

The key duties of the Committee include to:

• Monitor the integrity of the quarterly financial statements of the Company and any formal announcements relating to the Company’s financial performance, reviewing significant financial reporting judgements contained in them;
• Review the effectiveness of the Company’s internal financial controls, internal control and risk management systems;
• Monitor and review the effectiveness of the Company’s internal audit function;
• Make recommendations to the Board, for it to put to the shareholders for their approval in general meetings, in relation to the appointment, reappointment and removal of the external auditor and to approve the remuneration and terms of engagement of the external auditor;
• Review and monitor the external auditor’s independence and objectivity and the effectiveness of the audit process, taking into consideration relevant professional and regulatory requirements;
• Develop and implement policy on the engagement of the external auditor to supply non-audit services, taking into account relevant ethical guidance regarding the provision of non-audit services by the external audit firm and to report to the Board, identifying any matters in respect of which it considers that action or improvement is needed and making recommendations as to the steps to be taken; and
• Establish and maintain procedures for processing complaints regarding accounting, internal controls or auditing matters and to review the Company’s procedures for the confidential anonymous submission by Company employees of concerns regarding questionable accounting or auditing matters.

Items reviewed during the year included:

Financial reporting
The Committee reviewed the draft annual and interim management reports before recommending their publication to the Board. The Committee discussed with the Chief Executive, Chief Financial Officer and external auditor the significant accounting policies, estimates and judgements applied in preparing these reports. The Committee also reviewed the draft interim management statements.

Going concern and liquidity risk
The Committee reviewed in detail the Financial Reporting Council’s guidance for Directors in relation to going concern and liquidity risk published in October 2009 as well as its paper entitled Challenges for Audit Committees arising from current economic conditions published in November 2009. This year there has been continued strong focus on debt and liquidity management.

Internal control and risk management
The Committee reviewed the risk management process and discussed the inherent risks faced by the business. Risk management activities take place throughout the organisation to support the Committee in its corporate governance responsibilities, working with the business to proactively and effectively manage risk. This, together with the related controls and assurance processes, is designed to identify, evaluate and manage risk and to ensure that the resultant residual risks meet the risk appetite of the Board. The principal risks and uncertainties are outlined in the relevant section on pages 33 and 34. The Committee discussed with management how they would continue to deliver high-quality oversight and risk evaluation against the background of the current economic climate.

The Committee has an ongoing process for reviewing the effectiveness of the system of internal controls and of the internal audit function. During 2009/10, it reviewed and approved the risk-based audit plan and the staffing levels in Internal Control to ensure it had sufficient resources to fulfil the agreed plan. It considered reports from the Internal Control team summarising the audit findings and recommendations and describing actions taken by management to address any shortfalls. It reviewed the level and nature of outstanding audit weaknesses and invited management to the Committee to further understand progress where it felt it was necessary. It also reviewed how the audit function was performing against the relevant standards published by the Institute of Internal Auditors.
The business recently introduced an updated anti-fraud policy which provides greater clarity and guidance in respect of British Airways’ expectations of its employees. This revised code has been supported by a mandatory training course for all management colleagues which will be rolled out further in the organisation in future.

External audit
The Committee reviewed the external audit strategy and the findings of the external auditor from its review of the interim announcement and its audit of the annual financial statements. The Committee also reviewed the scope and costs of the external audit. The Committee has a clear policy regarding non-audit services that may be provided by the external auditor, which prohibits certain categories of work and controls the overall level of expenditure. Pre-authorisation is required for all non-audit work.

Whistleblowing
The confidential helpline run by Safecall, which allows employees to raise concerns, is working well and confidence in it is growing. The Committee received regular reports on the confidential reporting system to ensure that the Company’s whistleblowing processes are working appropriately. The Committee also received a report for the first time on the work of the Company’s network of harassment advisors.

Auditor independence
The Committee reviews the work undertaken by the external auditor and each year assesses its independence, objectivity and performance. In doing so, it takes into account relevant professional and regulatory requirements and the relationship with the auditor as a whole, including the provision of any non-audit services. The Committee monitors the auditor’s compliance with relevant regulatory, ethical and professional guidance on the rotation of partners, as well as assessing annually its qualifications, expertise, resources and the effectiveness of the audit process, including a report from the external auditor on its own internal quality procedures. Having reviewed Ernst & Young’s performance in 2010, the Committee decided it was in the Group’s and shareholders’ interest not to tender the external audit in 2010 and recommends the re-appointment of Ernst & Young LLP.

Audit Committee effectiveness
The Committee prepares and reviews with the Board an annual performance evaluation of the Committee. The findings of the review ensure that the Board is satisfied that the Committee is operating effectively, and meeting all applicable legal and regulatory requirements.

Other issues
Details of the fees paid to the external auditor during 2009/10 can be found in note 6 to the financial statements.

The terms of reference of the Committee are reviewed at least annually and any changes are recommended to the Board.