

# **Abengoa Audit and Control Committee**

# Abengoa Audit and Control Committee

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## Introduction

The year 2003 was the first full year in which the Audit Committee performed its functions as such. This Activity Report is intended to inform the general public and, more particularly, the shareholders of the activities that Abengoa carries out in this area.

For the Board of Directors to perform its functions in a strong and efficient manner, specialized Commissions must be created within the Board, in order to diversify the work and ensure that, in certain important issues, the proposals and resolutions have previously been approved by a specialized body that is able to filter and obtain information on its decisions, so as to strengthen the guarantee that the resolutions are objective and have been given due consideration.

The Audit Committee was, therefore, created as an informative and consultative body reporting to the Board of Directors. Its is authorized to inform, supervise and propose certain actions relating to issues that fall within the area of its competency.

Abengoa's Audit Committee was created by the Board of Directors of Abengoa, S.A. on December 2, 2002 under article 44 of the By-Laws, in order to meet the provisions on the Audit Committee set forth in Law 44/2002 on the Reform of the Financial System. Its Internal Regime Regulations were approved by the Board of Directors on February 24, 2003. Both these events were duly notified to the Stock Market National Commission as relevant facts.

The Audit Committee is, in its totality, formed by non-executive Board Members, its current composition being as follows:

|           |                                 |
|-----------|---------------------------------|
| Chairman  | D. José L. Méndez López (*)     |
| Member    | D. José B. Terceiro Lomba       |
| Member    | D. José J. Abaurre Llorente     |
| Secretary | D. Miguel Angel Jiménez-Velasco |

(\*) Representing the legal person Corporación Caixa Galicia, S.A.U. as a Director.

During the year 2003, the Audit Committee met 9 times.

We describe the Internal Regime Regulations that govern the operation of the Committee, the matters that fall within its competency and the activities carried out during the year below:

## Audit Committee Internal Regime Regulations

- Composition and Appointment:

The Audit Committee Regulations establish that it shall be formed permanently by three members of the Board of Directors. At least two of them will be non-executive Board Members, thus complying with the majority of non-executive members provided for in Law 44/2002.

Members shall be appointed for a maximum term of office of four years, which may be renewed for further terms of the same duration.

- Chairman and Secretary:

The Audit Committee will initially elect its Chairman from among all its members who are non-executive Board Members. The Chairmanship will be taken in turns, on an annual basis, by the non-executive Board Members that form part of the Committee and at least one year must elapse before the same Board Member is re-elected as Chairman.

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The Secretary to the Board of Directors shall act as Secretary to the Committee.

- Functions and Competencies:

The functions and competencies of the Audit Committee are as follows:

1. To inform on the Annual Accounts and the six-monthly and quarterly Financial Statements that must be sent to the market regulatory or supervisory bodies, mentioning the internal control systems, the control of the monitoring thereof and compliance therewith through internal audit and, when appropriate, the accounting principles applied.
2. To inform the Board of any change in accounting principles and the balance sheet and off-balance sheet risks.
3. To inform the General Shareholders' Meeting on the issues raised thereat by shareholders in relation to matters that fall within its competency.
4. To propose the appointment of the external Account Auditors to the Board of Directors, in order for the proposal to be submitted to the General Shareholders' Meeting.
5. To supervise the Internal Audit services. The Committee will have full access to the Internal Audit and will inform during the process of choosing, appointing, renewing and/or removing the manager thereof and fixing his remuneration, likewise informing on the budget of this Department.
6. To know the company's financial information system and internal control systems.
7. To be in contact with the external auditors to receive information on any issues that may jeopardize said auditors' independence and/or any other issues related to the account auditing process.
8. To call the Board Members it sees fit to attend to the Committee meetings, so that they can inform to the extent decided by the Committee.
9. To prepare an annual report on the Audit Committee's activities, which must be published together with the Annual Accounts for the year.

- Meetings and Notice:

The Audit Committee shall meet on the occasions required to perform the functions stated in the preceding article, which must be at least once a quarter. In general, the meetings will be held at the company's registered office, although the members may designate a different place for a specific meeting.

The Audit Committee shall also meet whenever a meeting is called by the Chairman, at his own initiative or at the request of any member of the Committee. Members of the Committee may, in any case, inform the Chairman of the advisability of including a certain matter on the Agenda of the following meeting. Notice shall be given sufficiently in advance, not less than three days, and in writing, including the Agenda. However, a meeting of the Audit Committee will be valid when all its members are present and they agree to hold the meeting.

- Quórum:

The Audit Committee shall be considered to have a valid quorum when a majority of its members are present. Attendance may only be delegated to a non-executive Board Member.

Its decisions will be validly adopted when the majority of the Committee members in attendance vote in favour. In the event of a tie, the Chairman shall have the casting vote.

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## Activities of the Audit Committee

The main activities submitted to the Audit Committee may be grouped into four different areas of competency:



### Verification of economic and financial information

The Group's financial information consists basically of the consolidated financial statements, drawn up quarterly, and the full consolidated Annual Accounts, drawn up annually.

This information is prepared on the basis of the account reporting that all the Group companies are obliged to submit for this purpose.

The information reported by each one of the individual companies is verified by both the Group's internal auditors and the external auditors, in order to ensure that the information is true and provides an accurate picture of the company.

Abengoa has made a significant effort to systemize the reporting systems to allow times to be reduced and the reports required to be prepared as automatically as possible. This is one of the Group's permanent objectives, which will allow a constant reduction in the times required to present the Group's financial information.

The Audit Committee's functions include the verification of the economic and financial information prepared by the Group before it is submitted to the Board of Directors of Abengoa and the regulatory bodies of the Stock Market National Commission.

Once the above requirements have been met, the information is made public for the market and the financial institutions.

### Supervision of the risk control system

Abengoa's risk control system is founded on two pillars: the Common Management Systems and the Internal Audit Services, the definitions, objectives, characteristics and functions of which are explained below.

Abengoa's Common Management Systems develop the company's internal rules and the risk evaluation and control method contained in these rules and represent a culture common to the management of Abengoa's businesses, sharing accumulated knowledge and fixing criteria and action guidelines.

Their objectives are described below:

- To identify possible risks, which, although any business involves them, we should try to be aware of and attenuate.

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- To optimize day-to-day management, applying procedures favouring financial efficiency, a reduction in expenses and the standardization and compatibility of information and management systems.
- To promote synergies and value creation by Abengoa's business groups, working in an environment of co-operation.
- To strengthen the corporate identity, with all the Abengoa companies respecting the shared values.
- To attain growth by strategic development seeking innovation and new options in the medium- and long-term.

The Systems cover the whole organization at three levels:

- all the Business Groups and areas of activity
- all levels of responsibility
- all kinds of operations

Meeting the provisions of the Common Management Systems is compulsory for the whole organization and, therefore, they must be known to all the members thereof. Any exceptions to these Systems must be made known to the person concerned and appropriately authorized.

The Common Management Systems are submitted to a permanent updating process, which allows the best practices to be included in each one of its fields of action. The successive updates to which they are submitted are immediately notified to the organization using computing media, which greatly facilitates the dissemination thereof.

In a group like Abengoa, with more than 200 companies, a presence in nearly 40 countries and approximately 9,000 employees, it is indispensable to define a common system for management of the business that permits working efficiently and on a coordinated and consistent basis.

The **Internal Audit Services** are structured around the Joint Audit Services, which include the audit teams of the Companies, Business Groups and Corporate Services and act in a coordinated manner, reporting to the Audit Committee of the Board of Directors.

From among their strategic objectives, we can highlight:

- Forestalling the audit risks of the Group's Companies, Projects and Activities, such as frauds, capital losses, operating inefficiencies and, in general, risks that may affect the favourable progress of the business.
- Controlling the application and promoting the development of appropriate and efficient management rules and procedures, in accordance with the Common Corporate Management Systems.
- Creating value for Abengoa, by promoting the building of synergies and the monitoring of optimal management practices.
- Coordinating and criteria and approaches of the work with the external auditors, seeking the greatest efficiency and profitability of both functions.

Therefore, the Internal Audit Services act through specific objectives:

- Evaluating the Audit Risk of Abengoa Companies and Projects following an objective procedure.
- Defining standard types of Internal Audit and Control work, in order to develop the pertinent Work Plans with the scope appropriate to each situation. The different types of work are linked to Audit Risk Evaluation, determine the Work Plans to be used and involve an appropriate type of Recommendations and Reports, meaning that, therefore, they should be used explicitly in said documents.

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- Guiding and coordinating the internal audit and control work planning processes of the Companies and Business Groups, defining a procedure for notification of said work and communication with the parties involved and establishing a coding system for the work, so that it can be appropriately controlled and monitored.
- Defining the process for communicating the results of each piece of audit work, the persons affected and the format of the documents in which it materializes.
- Reviewing the application of the plans, the appropriate performance and supervision of the work, the prompt distribution of the results and the monitoring of the recommendations and the implementation thereof.

The main objective is to control and reduce audit risk, defining this as any risk that affects the business and can be estimated, evaluated and/or controlled by Management.

Each Abengoa activity, project and company must have a preliminary audit risk evaluation that allows appropriate planning of the reviews to be performed. This risk estimate must follow objective criteria common to all the Group and will be the responsibility of the Internal Audit and Control Department, at the level of Joint Services that corresponds to each specific case.

Abengoa's main tool for risk prevention and control and for monitoring efficient processes is the Common Management Systems. The review of the application, implementation and development of these systems is a priority objective of the audit function, contributing not only the review facets, but also promotional and educational aspects, with a view to their being systematically employed by all Group personnel.

In relation to the above, the Internal Audit and Control function should exceed a mere supervisory approach and, without decreasing the inspection and review activity, should actively promote improvements with immediate repercussions on the optimization of processes and businesses, the obtaining of synergies and, in short, the creation of value for Abengoa.

In both the focus of the work and the planning, performance, documentation, programs and notification of results thereof, coordination with the external auditors should prevail, so that the work of the two functions is not duplicated and Abengoa's internal audit and control procedures are validated and may be deemed to be adequate audit proof to support the external auditor in his opinion.

To attain this objective, a standardization of all the work cycles and documentation that contribute to the consistency of the work of Abengoa's internal auditors will be fomented.

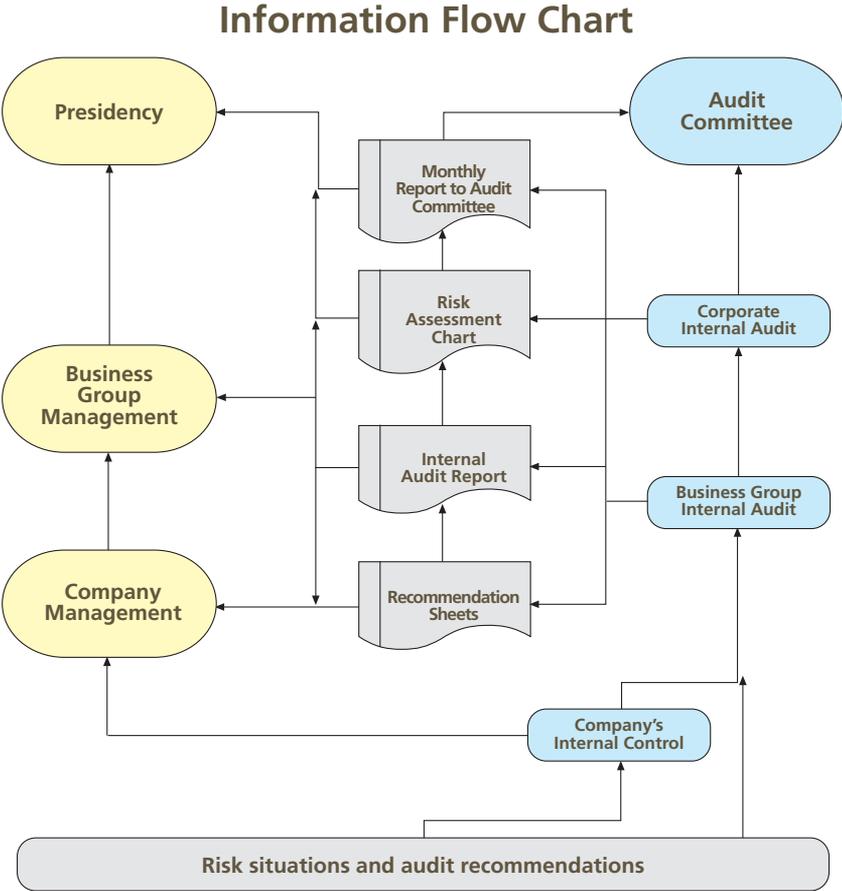
The external auditors must adopt an active attitude to improving the Group's controls and procedures, promoting the Internal Control Memorandum (issued upon conclusion of each job, with specific recommendations by area) as an end product of the audit work with great value for Abengoa.

The external auditors may perform internal audit functions when there are no Abengoa resources available. In these cases, the work, not the responsibility, will be delegated. In the course of these reviews they will, in principle, apply the Abengoa Internal Audit and Control work method and, only subsidiarily, that of their own firms.

Following the doctrine of The Institute of Internal Auditors and its Spanish branch, Instituto de Auditores Internos, the ultimate purpose of this structure is to provide the Management of Abengoa and of each of its Business Groups with an extra "control" flow of information, running parallel to the normal hierarchical flow, but with permanent horizontal information channels between each one of the hierarchical levels of the Companies and Business Groups and the pertinent Internal Audit services, applying clear and transparent criteria and safeguarding the confidential information involved.

# Abengoa Audit and Control Committee

This structure is shown in the following diagram:



Abengoa’s Internal Audit and Control Standard sets forth the way in which the Group’s Internal Audit activities are run in detail in the form of a Manual.

The Audit Committee’s functions include “to supervise the internal audit services” and “to know the financial information and “to know the company’s financial information system and internal control systems”.

The person responsible for Corporate Internal Audit informs the Committee systematically in relation to the Audit’s activities of:

- the Annual Internal Audit Plan and the extent to which it is met;
- the extent to which the recommendations issued have been implemented;
- an adequate description of the main areas reviewed and the most significant conclusions;
- any other more detailed explanations that the Audit Committee may require.

There are Audit Committees in other Group Companies, which are informed by the person responsible for Internal Audit in the relevant Business Group.

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## Compliance with the Annual Internal Audit Plan

The Annual Internal Audit Plan is drawn up each year and the scope thereof is determined by:

- the evaluation of the risk of the different companies, areas and projects
- the circumstances in each one of them at any given moment
- and the Audit Committee requirements

The evaluation of the audit risk is made for each project, company and Business Group. In this respect, audit risk is defined as any possible event that might have a negative effect on the business, such as fraud, capital losses or operating inefficiencies. The risk evaluation allows us to find out the areas on which we should focus our attention and work.

Planning seeks to guarantee that the risk areas identified will be covered by work that mitigates or eliminates the risks and allows them to be adequately identified, controlled and monitored. The result of this planning is the Annual Internal Audit Plan.

The Annual Plan establishes the types of work to be performed and the scope of each one of them. Depending on the proposed scope, general company reviews, reviews of specific areas, procedure review or special work are proposed.

The Annual Plan is continually monitored by the Audit Committee, which is informed systematically on both the progress thereof and the results obtained in the reviews performed.

For each of the tasks planned, once the field work has been performed, recommendations are identified that imply, not only that both legal and internal regulations are applied, but also that the best management practices in the pertinent area of activity are incorporated. These recommendations are classified as major or minor, depending on the importance of the area affected or, if applicable, the economic impact they imply.

In the year 2003, a total of 310 tasks were performed. The Annual Audit Plan for 2003 included 302 tasks and, thus, compliance was 103%. The eight extra tasks that were not included in the Plan relate mainly to Due Diligence carried out in processes to acquire companies or obtain holdings therein.

As a consequence of these tasks, 198 major recommendations were issued, 144 of which have already been implemented, while the remainder are in the process of implementation by the different companies.

## Monitoring the External Audit

The Audit Committee is responsible for supervising the results of the external auditors' work. It is, therefore, promptly informed of their conclusions and of any anomalies noted in the course of their reviews.

The external auditor must attend the Audit Committee when required to do so, in order to inform on the area of his competencies, mainly relating to:

- The review of the financial statements of the consolidated group and its companies and the issuance of an audit opinion thereon.

Although the scope of the opinion is the financial statements as of December 31 each year, the work performed by the auditors in each company includes a review of a previous accounting period end, usually that of the third quarter of the year (September), in order to anticipate any significant matters or operations that have arisen up to that date.

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- Evaluation of the Internal Controls

The advanced approach to auditing practice considers this to be part of an auditor's work, since this approach places more emphasis on the evaluations of the company's controls than on the substantive proof. In addition to their standard professional opinion, external auditors must issue an internal control report that is the basis of their presentation to the Audit Committee.

- Matters of special interest:

For certain specific matters or operations, an advancement of the auditors' opinion on the accounting principles adopted by the company is required, in order to reach a prior agreement on that principles.

Furthermore, the Audit Committee's functions include ensuring the independence of the external auditor and proposing the appointment or renewal thereof to the Board of Directors.

Abengoa, S.A.'s statutory auditor is PricewaterhouseCoopers, which is likewise the group's main auditor. Notwithstanding, a significant part of the Group, the part relating to the Environmental Services Business Group (Befesa), is audited by Deloitte. In addition, other audit firms also provide their services in small companies, both in Spain and abroad, although their scope cannot be called significant.

Abengoa's policy is for all group companies to be audited externally, even if they do not meet the requirements to make this compulsory.

The global amount of the fees agreed with the external auditors for the audit of the year 2003 and the distribution thereof is shown in the chart below:

|        | <b>Firm</b> | <b>Fees</b> | <b>Companies</b> |
|--------|-------------|-------------|------------------|
| Spain  | PWC         | 299,960     | 27               |
| Spain  | Deloitte    | 258,411     | 27               |
| Spain  | Other firms | 51,114      | 15               |
| Abroad |             | 446,590     | 57               |
| Total  |             | 1,056,075   | 126              |

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## Monitoring special projects

Either in the course of ordinary audit work or because of new circumstances, situations that require special treatment and monitoring may exist.

The Audit Committee is able to request work be carried out to meet specific objectives, or this work may arise at the initiative of Abengoa Management or the Internal Audit Department itself. In these cases, the Audit Committee will be especially informed of said situations, the measures that are being applied and the results obtained. They may include, among others:

- Significant risks:

When, due to the circumstance of a project or because of market changes, an important factor in creating the profit may be at risk, this must be handled separately and the Audit Committee must be systematically informed of the evolution thereof.

- Frauds:

Likewise, when, either due to an ordinary audit procedure or to specific information, a potential risk of fraud is known, a special review must be made and followed up, with systematic information to the Committee.

- Changes in legislation:

The existence of changes in the accounting or tax legislation may cause significant impacts on the financial statements of Abengoa and its group of companies and we must be in a position to anticipate this. Therefore, in these cases, special projects will be established in order to monitor the adaptation to and impact of the changes in detail. The Audit Committee shall be promptly informed and may be required to participate directly in the matter.

At present, we only have one project of this nature in progress and, given the importance thereof and its heavy impact on the Abengoa's financial statements, together with the period considered for implementation, will be especially monitored in the year 2004. It is the adaptation of Abengoa's financial statements to IAS (International Accounting Standards).

Although the adaptation to IAS will not be compulsory for listed groups of companies in Spain until exercises commenced later than January 1, 2005, Abengoa wishes to know the impact that this change will have on its financial statements and be in a position to issue converted financial statements, for information only, at the 2004 year end.

For this purpose, the Project of adaptation to IAS has begun, with the assistance of the group's auditors and an important assignment of group resources. This Project, which includes a first phase of diagnosis, a second phase of the detailed analysis of impacts and a last phase of implementation of the changes in the information systems, has already started and is forecast to conclude in the third quarter of the year 2004.

# Appointments and Remuneration Committee



# Appointments and Remuneration Committee

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The Appointments and Remuneration Committee was formed by the Board of the Directors of Abengoa on February 24, 2003, with approval, likewise, of its Internal Regulations.

## Composition

The current composition of the Committee, after inclusion, as independent members of the Board of Directors, of Mr. José B. Terceiro Lomba, Mr. Ignacio de Polanco Moreno and Mr. José Luis Méndez López (representing Corporación Caixa Galicia, S.A.U.) as a result of the resolutions adopted by the General Meeting of Shareholders of June 29, 2003, is as follows:

|                             |  |
|-----------------------------|--|
| - Ignacio de Polanco Moreno | Chairman. Independent Non-executive independent Director |
| - José B. Terceiro Lomba    | Member. Independent non-executive Director               |
| - José Luis Aya Abaurre     | Member. Shareholder representative                       |
| - José Marcos Romero        | Non-director Secretary                                   |

Consequently, the Appointments and Remuneration Committee is fully formed by non-executive Directors, thus exceeding the requirements established in the Financial System Reform Act. In addition, Chairmanship of the Committee is held by a non-executive Director, which is compulsory under the provisions of article 2 of the Committee's Internal Regulations.

## Functions

The functions and competencies of the Appointments and Remuneration Committee are:

1. To inform the Board of Directors on appointments, renewals, resignations and remuneration of members and Board of Directors and the Advisory Board and the holders of specific posts thereon and on the general remuneration and incentive policy for these bodies and for senior management.
2. To inform, previously, on all the proposals that the Board of Directors submits to the General Meeting in relation to the appointment or resignation of Directors, including co-option by the Board of Directors itself.
3. To prepare an annual report on the activities of the Appointments and Remuneration Committee, which must be included in the Directors' Report.

## Meetings

The Appointments and Remuneration Committee shall meet on the occasions required to meet the functions described above, at least once every six months.

In the year 2003, the Committee held two meetings specifically when the Ordinary General Meeting was called, in order to prepare the proposal for appointing directors and proposals to the Board of Directors for appointment of the members of the Board of Directors Advisory Committee.

# Appointments and Remuneration Committee

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## Organization and operation

The Committee shall be considered to have a valid quorum when a majority of its members are present. Attendance may only be delegated to a non-executive Director.

Its decisions will be validly adopted when the majority of the Committee members in attendance vote in favour. In the event of a tie, the Chairman shall have the casting vote.

The Company's Remuneration Manager attends the meetings of the Committee as the Secretary.

## Information presented to the Committee

- The Company's remuneration systems and criteria.
- Monitoring and evolution of remuneration.
- Proposal for remuneration of the members of the Board of Directors, the Board of Directors Advisory Committee and the Company's Senior Management.
- Preparation of the pertinent information to be included in the Annual Accounts.
- Proposal for the appointment of new directors; submission to the Ordinary General Shareholders' Meeting held on June 29, 2003 of the proposal for appointment of Mr. José Luis Méndez López, Mr. Ignacio de Polanco Moreno and Mr. José B. Terceiro Lomba as new directors, on the basis of their professional careers and experience, pursuant to the criteria fixed in the Regulations of the Board of Directors of Abengoa and the company By-laws. Proposal to the Board of Directors for the appointment of Mr. Maximino Carpio García and Mr. Daniel Villalba Vila as members of the Board of Directors Advisory Committee, due to their special technical qualifications and marked independence and professionalism.
- Proposal to the Board of Directors for the appointment of Mr. Carlos Sundheim Losada as a member of the Board of Directors Advisory Committee of Abengoa.