

## **AUDIT COMMITTEE**

### **Terms of Reference**

#### **Authority**

The Board has established a committee to be known as the Audit Committee (the Committee), which is a committee of the Board of Directors (the Board) from which it derives its authority and to which it is accountable. The Committee is authorised by the Board to:

- investigate any activity within its Terms of Reference.
- seek any information it requires from any employee. All employees are directed to co-operate with any reasonable request made by the Committee.
- commission internal investigations as it considers appropriate.
- obtain outside expert advice and support including legal advice and to secure the attendance of outsiders with relevant experience and expertise if it considers this necessary.

#### **Purpose**

The main functions and responsibilities of the Committee are to assist the Board in fulfilling its oversight responsibilities with specific regard to:

- Monitoring the integrity of the interim and annual financial statements and formal announcements relating to financial performance, focusing particularly on significant financial reporting judgments and ensuring the financial statements overall are fair, balanced and understandable.
- Reviewing the adequacy of systems of internal controls and the risk management systems.
- Scrutinising the activities and performance of the Internal Audit function.
- Monitoring the external auditors' independence and objectivity and the effectiveness of the audit process.
- Recommending the appointment and approving the remuneration and terms of engagement of the external auditors.
- Overseeing the Society's whistleblowing arrangements.

#### **Meetings and Membership**

Chairman	The Committee will be chaired by a Non-Executive Director (other than the Board Chairman) as appointed from time to time by the Board on the recommendation of the Nominations & Governance Committee. If the Chairman is absent at any meeting, the other Committee Members present will elect one of their number to chair the meeting.
Membership	The Committee will comprise the Audit Committee Chairman, the Board Risk Committee chairman and at least one other Member who will be appointed from the Non-Executive Directors (except for the Chairman of the Board) on the recommendation of the Nominations & Governance Committee in consultation with the Audit Committee Chairman. The Committee may operate with a vacancy. At least one member of the Committee should have recent and relevant financial experience with a professional qualification from one of the professional accountancy bodies.
Attendance	Only members of the Committee have the right to attend meetings. However the Chief Executive, Finance Director, Chief Risk Officer, the External Audit Partner and the Chief Internal Auditor shall normally attend meetings in their entirety. Other Board Members including the Chairman shall also have the right of attendance. Other senior managers may attend at the invitation of the Chairman of the Committee, but only for the duration of their presentation. At least once a year the Committee shall meet with the external auditors and, separately, with the Chief Internal Auditor without the Executive Directors present to discuss matters relating to their remit and any issues arising from the audit work they have undertaken.

Frequency	Meetings shall be held not less than four times a year. Any Member, the External Audit Partner or the Chief Internal Auditor may direct the Secretary to convene a meeting. Outside of the formal meeting programme, the Chairman of the Committee shall maintain a dialogue with key individuals involved in the Society's governance, including the Chairman, the Chief Executive, the Finance Director and the Chief Internal Auditor.
Quorum	Meetings of the Committee will be quorate if there are present at least two members of the Committee.
Secretary	The General Counsel and Secretary or their nominee shall be the Secretary of the Committee, except at such times when private discussion takes place between the Committee and external auditors.
Meeting preparation	The Secretary of the Committee shall draft the agenda for each meeting and provide this to the Chairman of the Committee for approval in advance of the meeting. The Secretary of the Committee shall collate the papers and issue to all attendees at least five days prior to the meeting. Meetings may be held in person or by telephone.
Reporting responsibilities	Formal minutes of the meetings of the Committee will be taken and circulated to members of the Committee. The Committee shall report to the Board on how it has discharged its responsibilities. Accordingly, minutes of Committee meetings will be submitted to the Board in the month following each meeting. In addition, the Chairman of the Committee will verbally report to the Board after each meeting of the Committee. The Chairman of the Committee or another of its members will be available at the Society's AGM to answer member questions on matters falling within the Committee's remit.

### **Duties**

The Committee shall carry out the following duties for the Society and its subsidiaries:

#### **Financial Reporting**

1. The Committee shall review the accuracy and integrity of the half-year and annual financial statements and any other formal announcements relating to financial performance of the Society prior to submission to the Board, focusing particularly on and challenging when necessary:
  - i) the consistency of, and any significant changes to, accounting policies and practices;
  - ii) significant financial reporting issues, estimates and judgments;
  - iii) significant adjustments resulting from the audit;
  - iv) the going concern assumption;
  - v) the adequacy of risk management arrangements, taking into account a report from the Chief Risk Officer;
  - vi) compliance with accounting standards and other relevant regulatory and legal requirements, taking into account the views of the external auditor.
2. The Committee shall advise the Board whether the Annual Report & Accounts, when taken as a whole, are fair, balanced and understandable and provide the information necessary for members to assess the Society's business model, strategy and performance.
3. The Committee shall report to the Board on how it has discharged its responsibilities in relation to the financial statements, including the significant issues that it considered and how they were addressed, and its review of the Society's Annual Report & Accounts and other financial statements including information presented with the financial statements such as the business review and corporate governance statements relating to audit and risk management.
4. The Committee shall approve a report of its activities for inclusion in the Society's Report and Accounts which shall include reference to:

- i) Its view of the effectiveness of the Internal Audit function.
  - ii) an explanation of how the Committee has assessed the effectiveness of the external audit process and the approach taken on the appointment or reappointment of the external auditor.
  - iii) details of the length of tenure of the existing external auditor.
  - iv) In the event the external auditor undertakes non-audit services for the Society, what arrangements are in place to ensure the objectivity and independence of the external auditor is safeguarded.
5. The Committee shall, in compiling such report for the Report and Accounts, include an explanation of the significant issues that the Committee considered in relation to the financial statements and how these issues were addressed and all other information requirements set out in the Corporate Governance Code.

#### **Internal Controls and Risk Management Systems**

6. The Committee shall review annually reports from the Internal Audit function regarding their assessment of the adequacy and effectiveness of the Society's systems of business and financial control and risk management systems, including the effectiveness of the Enterprise Wide Risk Management Framework and review and approve the statements to be included in the Annual Report & Accounts concerning internal control and risk management systems. The outcome of the review will be reported to the Board via the report regarding the financial statements.
7. The Committee shall consider the findings of internal investigations, together with management's response, that it has commissioned and any others that it reasonably considers relevant to its work.

#### **Internal Audit**

8. The Committee shall approve the appointment of the Chief Internal Auditor, after considering recommendations from the Chief Executive, and review any matters arising from the resignation or dismissal of the Chief Internal Auditor.
9. The Committee shall ensure that the Chief Internal Auditor has direct access to the Board Chairman, an independent reporting line to the Committee Chairman and is accountable to the Committee.
10. The Committee shall review and approve the Internal Audit function's remit, having regard to the complementary roles of the Internal Audit function and the external auditors.
11. The Committee shall review whether the internal audit function is adequately resourced, sufficiently independent, and has appropriate standing within the Society to fulfill its remit including monitoring.
12. The Committee shall oversee the performance of the Internal Audit function including assessing whether the function has the skills and resources available to undertake an audit of the Treasury function and is operating effectively as part of the Society's overall risk management framework in line with Policy Statement 7/15 issued by the PRA.
13. The Committee shall approve and monitor progress with the Internal Audit Annual Operational Plan.
14. The Committee shall receive reports from the Chief Internal Auditor, together with findings and recommendations for improvement (and, where necessary, to ensure the Board is made aware of significant issues).
15. The Committee shall monitor and review management's responsiveness to the internal audit findings and recommendations.

#### **External Audit**

16. The Committee shall consider and recommend to the Board the appointment, reappointment and removal of the external auditors. If relevant, the Committee shall investigate the issues arising from any resignation by an external auditor and consider what action is required as a result.
17. The Committee shall oversee the selection process for a new appointment of an external auditor of the Society, ensuring that the Society complies with the EU Audit Reform Directive and Regulation on mandatory firm rotation for public interest entities and other applicable legislation and codes of practice.
18. The Committee shall oversee the relationship with the external auditor including (but not limited to):

- i) assessing annually the qualification, expertise and resources of the external auditors.
  - ii) approving their remuneration, including both fees for audit and non-audit services, and ensuring that the level of fees is appropriate to enable an effective and high quality audit to be conducted;
  - iii) approving their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;
  - iv) reviewing and approving the annual audit plan and ensuring it is consistent with the scope of the audit engagement, having regard to the seniority, expertise and experience of the audit team;
  - v) reviewing the findings of the audit with the external auditor including discussing major issues which arose during the audit, levels of errors identified in the audit and the effectiveness of the audit process overall;
  - vi) assessing annually their independence and objectivity taking into account relevant UK professional and regulatory requirements and the relationship with the auditor as a whole, including the provision of any non-audit services;
  - vii) satisfying itself that there are no relationships between the auditor and the Society (other than in the ordinary course of business) which could adversely affect the auditor's independence and objectivity;
  - viii) monitoring the auditor's compliance with relevant ethical and professional guidance on the rotation of audit partner, the level of fees paid by the Society compared to the overall fee income of the firm and other related requirements; and
  - ix) reviewing the external auditor's management recommendations.
19. The Committee shall review audit representation letters and management letters and the responses of management to matters raised by the external auditor.
20. The Committee shall agree and monitor the Society's policies for the employment of former employees of the external audit firm and the engagement of the external auditor to supply non-audit services.

### **Whistleblowing**

21. The Committee shall oversee the arrangements by which the Society's staff may raise concerns about possible improprieties in matters of financial reporting or other matters (whistleblowing) and ensure that any such matter is properly investigated and followed up as required in line with the Society's Whistleblowing Policy and the relevant regulatory requirements. The Committee shall receive a report from the Whistleblowing Champion (as that term is defined in the Whistleblowing Policy) annually prior to such report being provided to the Board.
22. The Committee shall review the Society's procedures for detecting fraud and its systems and controls for the prevention of bribery.

### **Other Matters**

23. The Committee shall consider other topics, as defined by the Board.
24. The Committee shall undertake regular training including on financial reporting developments in order to keep its skills and relevant knowledge up to date.
25. The Committee shall undertake an annual assessment of its effectiveness and report the output of this assessment to the Board.

### **Annual Review**

The Committee Terms of Reference are reviewed at least annually by the Committee. Any changes are approved by the Board and the up-to-date Terms of Reference are included in the Board Governance manual and on the Society's website.

These terms of reference were approved by the Audit Committee on 8 December 2015 and by the Board on 18 December 2015