

TERMS OF REFERENCE – AUDIT, RISK AND COMPLIANCE COMMITTEE

Purpose

The purpose of the Committee is to ensure, and provide assurance to the Board that the Society's systems of control are appropriate in respect of the type of business it transacts, the market in which it operates and the regulatory regime by which it is assessed. In particular the Committee will review, approve and monitor internal audit strategies and reports, the external auditors' activities, the risk management strategies and exposure of the Society and its governance and regulatory compliance arrangements.

1. Membership

- 1.1 Members of the Committee shall be appointed by the Board, on the recommendation of the Nomination Committee in consultation with the Chairman of the Audit and Risk Committee. The Committee shall be made up of at least two members.
- 1.2 All members of the Committee shall be independent non-executive directors at least one of whom shall have recent and relevant financial experience. The Chairman of the Board shall not be a member of the Committee.
- 1.3 Only members of the Committee have the right to attend Committee meetings. However, other individuals such as the Chairman of the Board, Chief Executive, Chief Medical Officer, Finance Director, Financial Controller, Compliance Officer, the Actuaries and representatives from the management team may be invited to attend all or part of any meeting as and when appropriate.
- 1.4 Representatives from the external and internal auditors will be invited to attend meetings of the Committee on a regular basis.
- 1.5 Appointments to the Committee shall be for a period of up to three years, which may be extended for two further three year periods, provided the director remains independent.
- 1.6 The Board shall appoint the Committee Chairman who shall be an independent non-executive director. In the absence of the Committee Chairman and/or an appointed deputy, the remaining members present shall elect one of themselves to chair the meeting.

2. Secretary

- 2.1 The Company Secretary or his nominee shall act as the Secretary of the Committee.

3. Quorum

- 3.1 The quorum necessary for the transaction of business shall be two members. A duly convened meeting of the Committee at which a quorum is present shall be competent to exercise all or any of the authorities, powers and discretions vested in or exercisable by the Committee.

4. Frequency of Meetings

- 4.1 The Committee shall meet at least four times a year at appropriate times in the reporting and audit cycle and otherwise as required. Meetings may be held in person, over the telephone or by technology enabled conference.

5. Notice of Meetings

- 5.1 Meetings of the Committee shall be summoned by the Secretary at the request of any of its members or at the request of external or internal auditors if they consider it necessary.
- 5.2 Unless otherwise agreed, notice of each meeting confirming the venue, time and date shall be provided to each member of the Committee and any other person required to attend, no later than ten working days before the date of the meeting. Details of the agenda of items to be discussed, together with supporting papers, shall be forwarded to Committee members and to other attendees, as appropriate, no later than five working days before the date of the meeting.

6. Minutes of Meetings

- 6.1 The Secretary shall minute the proceedings and resolutions of all meetings of the Committee, including recording the names of those present and in attendance.
- 6.2 The Secretary shall ascertain, at the beginning of each meeting, the existence of any conflicts of interest and minute them accordingly.
- 6.3 Minutes of Committee meetings shall be circulated within ten working days of the meeting to all members of the Committee and, once agreed, to all members of the Board unless a conflict of interest exists.

7. Annual General Meeting

- 7.1 The Chairman of the Committee shall attend the Annual General Meeting prepared to respond to any member questions on the Committee's activities.

8. Duties

The Committee should carry out the duties below for the Society, its subsidiaries and the group as a whole, as appropriate.

8.1 Financial Reporting

- 8.1.1 The Committee shall monitor the integrity of the financial statements of the Society, including its Annual Reports and any other formal announcement relating to its financial performance, reviewing significant financial reporting issues and judgements which they contain. The Committee shall also review summary financial statements and significant financial returns to regulators.

- 8.1.2 The Committee shall review and challenge where necessary:
 - 8.1.2.1 the consistency of, and any changes to, accounting policies both on a year on year basis and across the Society/group;
 - 8.1.2.2 the methods used to account for significant or unusual transactions where different approaches are possible;
 - 8.1.2.3 whether the Society has followed appropriate accounting standards and made appropriate estimates and judgments, taking into account the views of the external auditor;
 - 8.1.2.4 the clarity of disclosure in the Society's financial reports and the context in which statements are made; and
 - 8.1.2.5 all material information presented with the financial statements, such as the operating and financial review and the corporate governance statement (insofar as it relates to the management of audit and risk).
- 8.1.3 The Committee shall review the annual financial statements of the defined benefit pension scheme where not reviewed by the Board as a whole.
- 8.1.4 The Committee shall make recommendations to the Board enabling the Board to finalise and sign statutory reports and other returns required of it.

8.2 Internal Controls and Risk Management Systems

The Committee shall:

- 8.2.1 review and recommend to the Board the Society's risk appetite together with any actions relating thereto;
- 8.2.2 review the Operational Risk Register to ensure that all actions necessary to mitigate risks have been maintained;
- 8.2.3 keep under review the effectiveness of the Society's internal controls and risk management systems;
- 8.2.4 review the integrity of the Society's internal financial reporting;
- 8.2.5 review and approve the statements to be included in the Annual Report concerning internal controls and risk management;
- 8.2.6 review the Society's FSA Returns (including the reconciliation of the Returns to the statutory accounts) and to recommend them to the Board for approval;
- 8.2.7 to review, and be satisfied in respect of, the work undertaken to prepare the Society's ICA prior to any discussion of the ICA by the Board;
- 8.2.8 keep abreast of both current risk management techniques and theories and any probable or actual changes in the regulatory environment, recommending action accordingly;
- 8.2.9 react to extreme market situations; and
- 8.2.10 evaluate the impact of change on existing activities and the likely risk involved in new ventures.

8.3 Whistle-blowing and Fraud

The Committee shall:

- 8.3.1 review the Society's arrangements for its employees to raise concerns, in confidence, about possible wrongdoing in financial reporting or other matters. The Committee shall ensure that these arrangements allow proportionate and independent investigation of such matters and appropriate follow up action; and
- 8.3.2 review the Society's procedures for detecting fraud.

8.4 Governance Arrangements and Regulatory Compliance

The Committee shall:

- 8.4.1 recommend to the Board the Society's attitude towards governance and regulatory compliance;
- 8.4.2 provide oversight of the Society's governance and regulatory compliance arrangements, and its related policies and procedures, and monitor their effectiveness;
- 8.4.3 keep under review developments and prospective changes in the regulatory environment;
- 8.4.4 keep under review developments in the Annotated Combined Code for Mutual Insurers and monitor the Society's compliance with the Code's principles and guidance (*with the exception of those that relate to responsibilities delegated specifically to the Nomination and Remuneration Committees*);
- 8.4.5 review the Report of the Directors on Corporate Governance to be included in the Society's Annual Report and Accounts and make a recommendation to the Board regarding its acceptance;
- 8.4.6 review and assess the effectiveness of the Society's systems of non-financial internal controls; and
- 8.4.7 make recommendations to the Board as to how the Society should engage effectively with its membership.

8.5 Internal Audit - Planning

The Committee shall:

- 8.5.1 be kept abreast of both current internal audit techniques and theories and any possible or actual changes in regulatory environment, discuss the impact of the same on the Society and recommend the necessary actions to be taken;
- 8.5.2 review and approve the utilisation of alternative strategies for internal audit;
- 8.5.3 monitor and review the effectiveness of the Society's internal audit arrangements in the context of the Society's overall risk management system;
- 8.5.4 approve the appointment and removal of the internal auditors;
- 8.5.5 consider and approve the remit of the internal auditors and ensure they have appropriate access to information to enable it to perform its function effectively and in accordance with the relevant professional standards;

- 8.5.6 annually review in conjunction with the internal auditors the Society's audit universe based on the risk appetite and risk controls in place;
- 8.5.7 review and assess the annual internal audit plan; and
- 8.5.8 agree with the internal auditors and review annually a basis of scoring internal audit reports which reflects the level of assurance given by the internal audit that risks are being controlled.

8.6 Internal Audit - Activity

The Committee shall:

- 8.6.1 review promptly all reports from the internal auditors above a green rating and others as appropriate;
- 8.6.2 review and monitor management's responsiveness to the findings and recommendations of the internal auditor and ensure that the agreed actions have been put into effect;
- 8.6.3 review at each meeting all outstanding audit actions based on a report received from the internal auditors; and
- 8.6.4 meet the internal auditors at least once a year, without management being present, to discuss their remit and any issues arising from the internal audits carried out. In addition the internal auditors shall be given the right of direct access to the Chairman of the Board and to the Committee.

8.7 External Audit

The Committee shall:

- 8.7.1 consider and make recommendations to the Board, to be put to members for approval at the AGM, in relation to the appointment, re-appointment and removal of the Society's external auditor. The Committee shall oversee the selection process for new auditors and if an auditor resigns the Committee shall investigate the issues leading to this and decide whether any action is required;
- 8.7.2 oversee the relationship with the external auditor including (but not limited to):
 - 8.7.2.1 approval of their remuneration, whether fees for audit or non-audit services and that the level of fees is appropriate to enable an adequate audit to be conducted;
 - 8.7.2.2 approval of their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;
 - 8.7.2.3 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;
 - 8.7.2.4 satisfying itself that there are no relationships (such as family, employment, investment, financial or business) between the auditor and the Society (other than in the ordinary course of business);
 - 8.7.2.5 agreeing with the Board a policy on the employment of former employees of the Society's auditor, then monitoring the implementation of this policy;

- 8.7.2.6 monitoring the auditor's compliance with relevant ethical and professional guidance on the rotation of audit partners, the level of fees paid by the Society compared to the overall fee income of the firm, office and partner and other related requirements;
 - 8.7.2.7 assessing annually their qualifications, expertise and resources and the effectiveness of the audit process which shall include a report from the external auditor on their own internal quality procedures;
 - 8.7.2.8 seeking to ensure co-ordination with the activities of internal audit;
 - 8.7.3 meet regularly with the external auditor, including once at the planning stage before the audit and once after the audit at the reporting stage. The Committee shall meet the external auditor at least once a year, without management being present, to discuss their remit and any issues arising from the audit;
 - 8.7.4 react to change in both the Society and market situations from an Audit and Risk Committee perspective;
 - 8.7.5 evaluate the impact of change on existing activities and the likely impact involved in new ventures;
 - 8.7.6 review and approve the annual audit plan and ensure that it is consistent with the scope of the audit engagement;
 - 8.7.7 review the findings of the audit with the external auditor. This shall include but not be limited to, the following:
 - 8.7.7.1 a discussion of any major issues which arose during the audit;
 - 8.7.7.2 any accounting and audit judgements; and
 - 8.7.7.3 levels of errors identified during the audit;
- The Committee shall also review the effectiveness of the audit.
- 8.7.8 review any representation letter(s) requested by the external auditor before they are signed by management;
 - 8.7.9 review the management letter and management's response to the auditor's findings and recommendations; and
 - 8.7.10 develop and implement a policy on the supply of non-audit services by the external auditor, taking into account any relevant ethical guidance regarding the provision of non-audit services by the external audit firm.

8.8 Compliance Audit

The Committee shall:

- 8.8.1 review the adequacy of the Society's compliance arrangements;
- 8.8.2 make recommendations for improvement;
- 8.8.3 monitor and review the effectiveness of the compliance audit function;
- 8.8.4 review the compliance audit programme and ensure that the compliance audit function is adequately resourced and has appropriate standing within the Society;

- 8.8.5 review and approve compliance audit reports and to consider management's response to report recommendations;
- 8.8.6 be kept abreast of both current compliance audit techniques and theories and any possible or actual changes in regulatory environment, recommending action accordingly; and
- 8.8.7 review and approve the utilisation of alternative strategies for compliance audit.

8.9 Reporting Responsibilities

- 8.9.1 The Committee Chairman shall report formally to the Board on its proceedings after each meeting on all matters within its duties and responsibilities.
- 8.9.2 The Committee shall make whatever recommendations to the Board it deems appropriate on any area within its remit where action or improvement is needed.
- 8.9.3 The Committee shall compile a report to members on its activities to be included in the Society's Annual Report.

8.10 Other Matters

The Committee shall:

- 8.10.1 have access to sufficient resources in order to carry out its duties, including access to the company secretariat for assistance as required;
- 8.10.2 be provided with appropriate and timely training, both in the form of an induction programme for new members and on an ongoing basis for all members;
- 8.10.3 give due consideration to laws and regulations, the provisions of the Combined Code and related guidance as appropriate;
- 8.10.4 be responsible for co-ordination of the internal and external auditors;
- 8.10.5 oversee any investigation of activities which are within its terms of reference and act as a court of the last resort;
- 8.10.6 make available to members the Committee's terms of reference, which should set out the Committee's role and delegated responsibilities and be reviewed and, where necessary, updated annually; and
- 8.10.7 at least once a year, review its own performance, constitution and terms of reference to ensure it is operating at maximum effectiveness and recommend any changes it considers necessary to the Board for approval.

9. Authority

The Committee is authorised:

- 9.1 to seek any information it requires from any employee of the Society in order to perform its duties;
- 9.2 to obtain, at the Society's expense, outside legal or other professional advice on any matter within its terms of reference; and
- 9.3 to call any employee to be questioned at a meeting of the Committee as and when required.