

THE CHILDREN'S MUTUAL
AUDIT AND RISK COMMITTEE
TERMS OF REFERENCE

1. PURPOSE AND CONSTITUTION

- 1.1 The Audit and Risk Committee (“the Committee”) shall be responsible on behalf of the Board, for the oversight of risk management, risk appetite, regulatory capital, the external auditors, financial reporting, internal control and internal audit, and certain regulatory and compliance matters. It will do so with the objective of ensuring that the Society complies with all legal and regulatory requirements relating to these matters and with generally accepted standards appropriate for an organization of its size and complexity.
- 1.2 In pursuit of these objectives, the Committee may have certain decisions delegated to it by the Board and may make recommendations as it sees fit to the Board.
- 1.3 The Board, on the recommendation of the Nomination Committee, shall appoint the Committee and its Chairman. The Committee shall consist exclusively of non-executive Directors and shall comprise at least three such Directors.
- 1.3 The Chairman of the Board shall not be Chairman of the Committee. At least one member of the Committee should have recent and relevant financial experience.

2. PROCEDURE

- 2.1 The Committee shall meet as and when it deems necessary; provided that it shall meet at least four times each year.
- 2.2 Any two members of the Committee shall comprise a quorum.
- 2.3 In the absence of the Chairman of the Committee from any particular meeting, the remaining members present shall elect one of their number present to chair the meeting.
- 2.4 At least once a year, the Committee shall meet the:-
- external auditors without the executive management present;
 - Head of Audit and Risk Management Services without the executive management present; and
 - Regulation and Risk Director without the executive management present.

The auditors, Head of Audit and Risk Management Services and the Regulation and Risk Director may each at any time communicate directly with the Chairman of the Committee and may request a meeting with the Committee.

- 2.5 The Committee shall put in place such procedures as it considers necessary to ensure that any conflicts that could arise from its oversight of both the risk and audit functions are satisfactorily managed.
- 2.6 The Committee may request the attendance at its meetings, either by a standing invitation or specific request, any Director or employee of, or adviser to, the Society, but the invitees have no right of attendance. Right of attendance is only extended to

other Society Non-Executive Directors. The Regulatory and Risk Director and the Internal Audit Manager shall generally be expected to attend meetings of the Committee, unless requested otherwise.

- 2.7 Any Director who is not a member of the Committee may request to attend meetings of the Committee and shall generally be permitted to do so except for executive Directors at meetings or parts of meetings when the Committee requests that no executive management is present, but shall have no right to do so if the Committee decides otherwise.
- 2.8 The Company Secretary, or a deputy, shall act as Secretary to the Committee.
- 2.9 Minutes of Committee meetings shall be circulated to the Committee, in draft, immediately following their approval for circulation by the Chairman of the Committee and, in final form, to all members of the Board with the next set of Board papers following their approval.
- 2.10 The Chairman of the Committee, after each meeting, shall make a report to the following Board meeting.

3. AUTHORITY

The Committee is authorised by the Board to investigate any activity within its terms of reference. The Committee is authorised to obtain independent professional advice where necessary, at the Society's expense, and to require the provision of any information from any Director or employee of the Society.

4. DUTIES

The duties of the Committee are:

a) *Auditors*

- i. to make recommendations to the Board for members to consider at the AGM in relation to the appointment, reappointment and, if ever applicable, removal of the external auditors (the "auditors");
- ii. to review at least annually and monitor the independence and objectivity of the auditors and the scope and effectiveness, including cost effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements;
- iii. to review and agree with the auditors their Audit Engagement Plan (or equivalent document) in advance of the commencement of each audit;
- iv. to develop and implement policy on the engagement of the external auditor to supply non-audit services, taking into account relevant guidance regarding the provision of non-audit services by the auditors;
- v. to approve on behalf of the Board the remuneration and terms of engagement of the auditors, both in respect of their audit and material non-audit services.

b) *Financial and regulatory reporting*

- i. to ensure that the integrity of the financial statements of the Company is maintained, focusing particularly on the following matters:
 - (1) accounting policies and practices and any changes thereto;
 - (2) significant financial reporting judgements contained or implied in them, including the methodology, appropriateness and consistency of any material provisions or reserves, including the reserves held for insurance liabilities as recommended by management;
 - (3) significant adjustments, if any, resulting from audit or auditors' review;
 - (4) the going concern assumption;
 - (5) disclosures in the financial statements, including risks and uncertainties;
 - (6) compliance with accounting standards;
 - (7) the statutory valuation assumptions, the statutory valuation results, and the Society's FSA returns.
- ii. to make such comments and / or recommendations as considered necessary to the Board regarding the approval of the financial statements; and
- iii. to consider the external auditor's management letter, approve management's response and oversee the implementation of agreed actions.

c) *Capital Management*

- i. to oversee the regular updating of the Society's ICA report for approval by the Society's Board;
- ii. to review the adequacy and appropriateness of stress and scenario tests (including reverse stress testing) linked to the capital setting exercise and where appropriate to recommend any further stress or scenario tests necessary;
- iii. review the effects on capital as a result of specific events occurring and / or instances where assumptions material to the Society's business plan are compromised and make recommendations to the Board as considered appropriate.

d) *Risk management*

- i. to review quarterly the risk exposures facing the Company as well as the actions being taken to manage and/or mitigate these risks;
- ii. to consider the completeness of the risk profile presented and evaluate potential emerging or new risk issues facing the Company;
- iii. to consider whether risk exposures are being managed within agreed risk tolerances and to review the adequacy of management actions and plans where levels of risk are in excess of tolerances;
- iv. to challenge whether additional actions may be necessary to mitigate material risk exposure or respond to emerging risk issues;
- v. to review and consider the Company's stated risk appetite, tolerances and policies by reference to current and relevant information and to make such recommendations to the Board thereon as considered necessary;
- vi. to assist the Committee in its consideration of the above, the Committee will receive reports which will include the following:

- a) a report of risk exposures measured against agreed tolerances;
- b) details of the risk assessment process that has been carried out across the Company and a confirmation by the Regulation and Risk Director either that it has been conducted satisfactorily according to required standards and accuracy or, if not, the areas of deficiency;
- c) a statement as to whether approved risk policies, appetites and standards have been complied with and, in the event of any breaches, what actions have been taken or are planned to address them; and
- d) a summary of any significant risk events and material near misses which might have resulted in risk tolerances being exceeded.

e) *Internal Audit*

- i. to monitor and review the effectiveness of the internal audit function with particular regard to availability of resource and standing in the business;
- ii. to agree an effective internal audit programme with the Head of Audit and Risk Management Services;
- iii. to discuss and consider problems and reservations arising from audits, including internal audits, and any matters which the Head of Audit and Risk Management Services may wish to discuss (in the absence of other executive management if appropriate);
- iv. to review and consider internal audit findings and any management responses thereto and to consider the progress of corrective action agreed by management;
- v. to agree the framework for regular review of the effectiveness of internal control (including financial, operational and compliance controls) having regard to:
 - (1) the risks faced by the Company;
 - (2) corporate developments and changes in the business environment in which the Society operates;
- vi. to review on an annual basis the statement on internal control to be included in the corporate governance statement in the annual report and accounts prior to its endorsement by the Board, and specifically to review:
 - (1) procedures for identifying and controlling the risks faced by the Society;
 - (2) The Society's policies for ensuring that it complies with relevant regulatory and legal requirements; and
 - (3) the effectiveness of internal control.

f) *Regulatory and compliance*

- i. to monitor and review the effectiveness of Compliance, both generally and against the stated roles and responsibilities of Compliance;
- ii. to agree an effective annual compliance programme with the Compliance Officer;

- iii. to review reports on the Company by the FSA, or any other regulator and to review the Company's compliance with relevant regulations;
- iv. to receive and review the Compliance monitoring reports quarterly, or as they are issued, and to discuss and consider problems and reservations arising from compliance monitoring.

g) Other

- i. to review arrangements by which staff may, in confidence raise concerns about possible improprieties in matters of financial reporting or other matters, with the objective of ensuring that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action (whistleblowing);
- ii. to evaluate its own collective performance at least annually;
- iii. to review annually these terms of reference and either recommend changes to the Board or confirm to the Board that no changes are required;
- iv. to report on its work annually in the Company's Annual Report;
- v. to consider the nature, quality and timeliness of risk management information provided to the Board;
- vi. to report back any relevant conclusions, concerns or advice of the Committee to the Board; and
- vii. to consider other topics that may be referred to it by the Board.

In respect of all such matters, reporting to the Board as appropriate, identifying any matters in respect of which it considers that action or improvement is needed, and making recommendations to the Board as to the steps to be taken.