

**PENNON GROUP PLC
(the "Company")**

**AUDIT COMMITTEE (the "Committee")
TERMS OF REFERENCE**

1. COMPOSITION

1.1 Membership

- Members will be appointed by the Board, on the recommendation of the Nomination Committee in consultation with the Chair of the Audit Committee and in accordance with the Company's articles of association.
- The Committee shall be made up of at least three members all of whom shall be independent non-executive directors.
- One of the members shall have recent and relevant financial experience ideally with a professional qualification from one of the professional accounting bodies. The other members shall have the requisite degree of financial knowledge and experience to provide appropriate challenge.
- The Committee as a whole shall have competence relevant to the sector in which the company operates.
- The Chair of the Board shall not be a member of the Committee.

1.2 Committee Chair

- The Committee Chair shall be appointed by the Board and shall be an independent non-executive director (but not the Chair of the Board).
- In the absence of the Committee Chair and/or an appointed deputy, the remaining members present shall elect one of themselves to chair the meeting.

1.3 Secretary

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

2. DUTIES AND RESPONSIBILITIES

In carrying out its responsibilities the Committee must act in accordance with the UK Corporate Governance Code (the "Code") and shall:

2.1 Financial Reporting

2.1.1 monitor the integrity of the financial statements of the Group, including:

- its Annual Report and Accounts;
- its half-yearly report and preliminary announcement of the final results;
- its quarterly trading updates; and
- any other formal announcements relating to its financial performance, reviewing and reporting to the Board on significant financial reporting issues and judgements which they contain.

2.1.2 review significant financial reporting issues and judgments which the above statements contain having regard to matters communicated by the auditor, and review and challenge in particular:

- the application of significant accounting policies, the quality and consistency of the policies, and any changes to them both on a year-on-year basis and across the Group;

- the methods used to account for significant or unusual transactions where different approaches are possible;
- whether the Group has followed appropriate accounting standards and made appropriate estimates and judgements, taking into account the views of the external auditor;
- the clarity and completeness of disclosure in the Group's financial reports and the context in which statements are made; and
- all material information presented with the Annual Report and Accounts, such as the strategic report, directors' report and the corporate governance statement and the other statements listed in 2.1.1 above, relating to financial information, audit, risk or internal controls.

2.1.3 review the content of the Annual Report and Accounts and the other statements listed in 2.1.1 above and advise the Board on:

- the assumptions or qualifications in support of the going concern statement to be included in the Annual Report (including any material uncertainties as to the Group's ability to continue adopting the going concern assumption); and
- whether the Annual Report and Accounts and the other relevant statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders and other key stakeholders to assess the Company's position and performance, business model and strategy.

2.1.4 Where the Committee is not satisfied with any aspect of the proposed financial reporting by the Company it shall report accordingly to the Board.

2.1.5 Where requested by the Board, provide advice on how, taking account of the Group's position and principal risks, the prospects of the Group have been assessed, over what period, and why that period is appropriate, and whether there is a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the chosen period, drawing attention to any qualifications or assumptions as necessary. This should subsequently be presented in the Annual Report.

2.1.6 The Committee shall monitor compliance with financial reporting and accounting standards and compliance with any stock exchange and other legal, governance and regulatory requirements.

2.2 Risk Management

The Committee shall (on behalf of the Board which retains overall responsibility for internal controls and risk management systems):

Internal controls and risk management systems

2.2.1 monitor internal control systems and the level of risk in the business, carrying out a review at least annually of the effectiveness of the systems, processes and policies established to identify, assess, manage and monitor the Company's internal controls, including financial, operational, compliance and general IT controls, and risk management processes, and their compliance with relevant laws, regulation and disclosures;

2.2.2 review, and recommend to the Board for approval, the statements to be included in the Annual Report and other statements listed in 2.1.1 above concerning internal control, principal and emerging risks, risk management, going concern and the viability statement;

2.2.3 monitor compliance with financial reporting and accounting standards and compliance with

any stock exchange and other legal, governance and regulatory requirements;

Risk management function and risk assessment and procedures

- 2.2.4 review the effectiveness of the risk management function (at least annually), and seek such assurance as it may deem appropriate that the function is adequately resourced and has appropriate standing within the Company, with the risk management process being appropriately embedded into the business and effectively operated;
- 2.2.5 ensure that a robust assessment of the emerging and principal risks facing the Company has been undertaken (including those risks that would threaten the Company's business model, future performance, solvency or liquidity and reputation);
- 2.2.6 ensure that procedures are in place to identify principal and emerging risks on a timely basis and provide advice on the management and mitigation of those risks;
- 2.2.7 assist the Board in monitoring the Company's risk profile and exposure, including overseeing the business' compliance with the risk appetite and tolerance set by the Board, taking account of the current prospective macroeconomic, financial and climatic environment and the Company's strategic objectives;
- 2.2.8 periodically review the effectiveness of the risk management framework and undertake in-depth reviews of high-risk business areas or processes as requested by the Board to understand key drivers, mitigation activity and further management activity; and

Risk and internal controls reporting

- 2.2.9 receive and review reports from management to support fulfilling the above responsibilities, including reports regarding:
 - assurance on the effectiveness of the internal control and risk management systems;
 - identifying and managing emerging and principal risks; and
 - material breaches of risk tolerance and appetite limits and the adequacy of proposed action.

The Committee will also consider reports from internal audit and external audit on the operational effectiveness of matters related to risk and control.

2.3 Fraud, Bribery and Corruption and Whistleblowing

The Committee shall:

- 2.3.1 review the policies on anti-bribery and corruption, whistleblowing and gifts and hospitality, and the systems and controls in place to prevent bribery and financial misconduct, and receive reports on any non-compliance with such policies, systems and controls annually.
- 2.3.2 review the Group's arrangements for its employees, contractors and external parties 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.
- 2.3.3 review the Group's procedures for detecting fraud; and

- 2.3.4 consider the major findings of any relevant internal investigation into fraud or financial misconduct and management's response.

2.4 Internal Audit

The Committee shall:

- 2.4.1 monitor and review the role and effectiveness of the Group's internal audit function in the context of the company's overall risk management system, its compliance and finance functions, and the work of the external auditor;
- 2.4.2 approve the appointment and removal of the Director of Risk and Assurance;
- 2.4.3 annually approve the Internal Audit Charter, confirming the remit of the internal audit function, ensuring the function has adequate resources and appropriate access to information to enable it to perform its function effectively, in accordance with the relevant professional standards, ensuring it is appropriate for the current needs of the organisation;
- 2.4.4 review and assess the annual internal audit plan to ensure it is aligned to the key risks of the business, and receive regular reports on work carried out;
- 2.4.5 review conclusions and manager responses and responsiveness to the findings and recommendations of the internal auditors;
- 2.4.6 ensure internal audit has unrestricted scope, the necessary resources and access to information to enable it to fulfil its mandate, ensure there is open communication between different functions and that the internal audit function evaluates the effectiveness of these functions as part of its internal audit plan, and ensure that the internal audit function is equipped to perform in accordance with appropriate professional standards for internal auditors;
- 2.4.7 meet the Director of Risk and Assurance 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 Director of Risk and Assurance shall be given the right of direct access to the Chair of the Board and to the Chair of the Committee, providing independence from the Executive and accountability to the Committee; and
- 2.4.8 carry out an annual assessment of the effectiveness of the internal audit function and as part of this assessment: meet with the head of internal audit without the presence of management to discuss the effectiveness of the function; review and assess the annual internal audit work plan; receive a report on the results of the internal auditor's work; determine whether it is satisfied that the quality, experience and expertise of internal audit is appropriate for the business; review the actions taken by management to implement the recommendations of internal audit and to support the effective working of the internal audit function; and consider whether an independent, third party review of processes is appropriate.

2.5 External Audit

The Committee shall:

- 2.5.1 consider and make recommendations to the Board, to be put to shareholders for approval at the AGM, in relation to the appointment, re-appointment and removal of the Group's external auditor;
- 2.5.2 ensure that the external audit services contract is put out to tender and the external auditor is changed in accordance with relevant regulation. The Committee shall develop and oversee the selection process for new auditors and ensure that all tendering firms have such

- access as is necessary to information and individuals during the tendering process;
- 2.5.3 if an auditor resigns or is dismissed, investigate the issues leading to this and decide whether any action is required;
 - 2.5.4 oversee the relationship with the external auditor including (but not limited to):
 - 2.5.4.1 agreeing 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;
 - 2.5.4.2 agreeing their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;
 - 2.5.4.3 assessing annually their independence and objectivity taking into account relevant law, regulation, the Financial Reporting Council's Ethical Standard and other professional requirements and the Group's relationship with the auditor as a whole, including any threats to the auditor's independence and the safeguards applied to mitigate those threats including the provision of any non-audit services;
 - 2.5.4.4 satisfying itself that there are no relationships (such as family, employment, investment, financial or business) between the auditor and the Group (other than in the ordinary course of business);
 - 2.5.4.5 agreeing with the Board a policy on the employment of former employees of the Group's auditor, as required, then monitoring the implementation of this policy, taking into account the FRC's Ethical Standard and current legal requirements;
 - 2.5.4.6 monitoring the auditor's processes for maintaining independence, its compliance with relevant law, regulation, other professional requirements and the Ethical Standard, including the professional guidance on the rotation of audit partners;
 - 2.5.4.7 monitoring the level of fees paid by the Group compared to the overall fee income of the firm, office and partner and assess these in the context of relevant legal, professional and regulatory requirements, guidance and the Ethical Standard; and
 - 2.5.4.8 assessing annually the qualifications, expertise and resources of the external auditor and the effectiveness of the audit process which shall include a report from the external auditor on their own internal quality procedures;
 - 2.5.5 seek to ensure coordination of the external audit with the activities of the internal audit function;
 - 2.5.6 evaluate the risks to the quality and effectiveness of the financial reporting process in the light of the external auditor's communications with the Committee;
 - 2.5.7 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;
 - 2.5.8 discuss with the external auditor the factors that could affect audit quality and review and approve the annual audit plan and ensure that it is consistent with the scope of the audit engagement, having regard to the seniority, expertise and experience of the audit team;
 - 2.5.9 review the findings of the audit with the external auditor. This shall include but not be limited to, the following:
 - 2.5.9.1 a discussion of any major issues which arose during the audit,

- 2.5.9.2 the auditor's explanation of how the risks to audit quality were addressed
 - 2.5.9.3 key accounting and audit judgements,
 - 2.5.9.4 the auditor's view of their interaction with senior management,
 - 2.5.9.5 levels of errors identified during the audit; and
 - 2.5.9.6 any reservations that the external auditors may have and other matters that they wish to raise.
- 2.5.10 review any representation letter(s) requested by the external auditor before they are signed by management giving particular consideration to matters where representation has been requested that relates to non-standard issues;
- 2.5.11 review the management letter and management's response to the auditor's findings and recommendations;
- 2.5.12 review the effectiveness of the audit process, including an assessment of the quality of the audit, the handling of key judgements, by the auditor, and the auditor' response to questions from the Committee; and
- 2.5.13 develop and recommend to the Board a policy on the supply of non-audit services by the external auditor. The policy should include consideration of the following matters:
- 2.5.13.1 threats to the independence and objectivity of the external auditor and any safeguards in place;
 - 2.5.13.2 the nature of the non-audit services;
 - 2.5.13.3 whether the external audit firm is the most suitable supplier of the non- audit service
 - 2.5.13.4 the fees for the non-audit services, both individually and in aggregate, relative to the audit fee; and
 - 2.5.13.5 the criteria governing compensation.
- 2.5.14 The Committee shall evaluate the risks to the quality and effectiveness of the financial reporting process and consider the risk of the withdrawal of the Group's present auditor from the market.

2.6 Policies and Oversight of other Matters:

- 2.6.1 The Committee shall review periodically:
- the Delegated Authorities Schedule;
 - the Group Risk Management policy and recommend any material changes for approval to the Board, as appropriate;
 - the Group Treasury policies and recommend any material changes for approval to the Board, as appropriate;
 - the Group's tax strategy and recommend any changes for approval to the Board as appropriate; and

- the Group's environmental and climate risk mitigation strategy, targets, progress and reporting, as relates to the Task Force on Climate-related Financial Disclosures.

3. REPORTING

3.1 To the Board

- The Committee Chair shall report formally to the Board on its proceedings after each meeting on all matters within its duties and how it has discharged its responsibilities.
- The Committee shall make whatever recommendations to the Board it deems appropriate on any area within its remit where action or improvement is needed.

3.2 Annual Report

The Committee shall compile a report to shareholders on its activities to be included in the Company's Annual Report, which shall include details of the number of meetings held and attendance over the course of the year. This report shall describe the work of the Committee, including:

- the significant issues that it considered in relation to financial statements and how these were addressed, having regard to matters communicated to it by the external auditor;
- an explanation of how the Committee has assessed the independence and effectiveness of the external audit process and the approach taken to the appointment or reappointment of the external auditor (including information on the length of tenure of the current audit firm, when a tender was last conducted and advance notice of any retendering plans); and
- an explanation of how auditor independence and objectivity are safeguarded if the external auditor provides non-audit services, having regard to the matters communicated to it by the auditor and all other information requirements set out in the Code.

3.2.1 In compiling the reports referred to in this section, the Committee should exercise judgement in deciding which of the issues it considers in relation to the financial statements are significant, but should include at least those matters that have informed the Board's assessment of whether the company is a going concern and the inputs to the Board's viability statement.

3.2.2 The Committee shall approve, for inclusion in the Annual Report, a statement of compliance with the provisions of the Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 and, if applicable, to produce a statement to include the disclosures required by Article 4 of that Order.

4. OTHER MATTERS

The Committee shall:

4.1 Evaluation

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.

4.2 **Training**

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.

4.3 **Auditors**

Be responsible for the oversight of the co-ordination of the internal and external auditors.

4.4 **Investigations**

Oversee any investigation of activities which are within its terms of reference and act as a court of the last resort.

4.5 **Best practice**

Give due consideration to laws, regulations and any published guidelines or recommendations including but not limited to the provisions of the UK Corporate Governance Code, the requirements of the FCA Listing, Prospectus and Disclosure Guidance and Transparency Rules as well as guidelines published by relevant institutional investors and representative bodies, and any other applicable rules as appropriate.

4.6 **Committees**

Work and liaise as necessary with all other Board Committees, taking particular account of the impact of risk management and internal controls being delegated to different Committees. In particular, provide advice to the Remuneration Committee on financial reporting matters and related judgements and risk management as they affect performance objectives incorporated in executive remuneration.

4.7 **Projects**

Undertake any other projects relating to its remit which it considers appropriate or as requested by the Board.

4.9 **Authority**

The Committee is authorised by the Board to:

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

5 **MEETING ARRANGEMENTS**

5.1 **Attendance**

- Only members of the Committee have the right to attend Committee meetings.
- However, other individuals including the Chair of the Board, Group Chief Executive Officer, Group Chief Financial Officer, Chief Operating Officer, the Director of Risk and Assurance, the Group Financial Controller, other representatives from Group Finance and

the External Auditors may be invited to attend all or part of any meeting as and when appropriate and necessary.

- The external auditors and the head of the internal audit function will be invited to attend meetings of the Committee on a regular basis.

5.2 Meetings

- 5.2.1 The quorum necessary for the transaction of business shall be two members of which at least one member shall have recent and relevant financial experience. 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.
- 5.2.2 The Committee shall meet at least four times a year in person or by telephone or video conference at appropriate times in the reporting and audit cycle and otherwise as required.
- 5.2.3 Meetings of the Committee shall be called by the Secretary of the Committee at the request of any of its members or at the request of external or internal auditors if they consider it necessary.
- 5.2.4 Unless otherwise agreed, notice of each meeting confirming the venue, time and date together with an agenda of items to be discussed, shall be forwarded to each member of the Committee, any other person required to attend and all other non- executive directors, no later than five working days before the date of the meeting unless agreed otherwise in advance. Supporting papers shall be sent to Committee members and to other attendees, as appropriate, at the same time and in a timely manner to enable full and proper consideration to be given to issues.
- 5.2.5 The Secretary will minute the proceedings of each meeting, which shall be circulated promptly to all members of the Committee and, once agreed, to all other members of the Board, unless it would be inappropriate to do so.
- 5.2.6 Conflicts of interest must be declared by members at the beginning of meetings and the Secretary shall record any such declaration in the minutes. If a matter that is considered by the Committee is one where a Committee member, either directly or indirectly, has a conflict of interest, that member shall not be permitted to vote at the meeting.

5.3 Resolutions and approvals

- 5.3.1 Committee resolutions shall be passed by the absolute majority of votes cast. In the event of equality of votes, the Committee Chair shall have the casting vote (except where he/she is not permitted to vote).
- 5.3.2 Approvals may be taken in written form (including email), or via telephone or video conference.
- 5.3.3 Approvals by email must be included in the minutes of the next meeting of the Committee.
- 5.3.4 The Committee has the delegated authority of the Board in respect of the functions and powers set out in these terms of reference. The Committee may sub-delegate any or all of its powers as it thinks fit to the Committee Chair or, if it considers it to be appropriate, to the Company Secretary.

5.4 Annual General Meeting

The Committee Chair shall attend the Annual General Meeting prepared to respond to any shareholder questions on the Committee's activities. In addition, the Committee Chair should seek engagement with shareholders on significant matters related to the Committee's area of responsibility.