

Severn Trent Plc Audit Committee

Terms of Reference (Approved by the Board on 20 April 2018)

1. Purpose

The purpose of the Committee is to establish formal and transparent policies and procedures to ensure the independence and effectiveness of internal and external functions as required by Provision C.3 of the UK Corporate Governance Code April 2016.

2. Constitution

The Board of Directors (the "Board") has established, in line with the UK Corporate Governance Code April 2016 (the "Code"), a Committee of the Board, by resolution of the Board, henceforth known as the Audit Committee (the "Committee").

3. Membership

- The Committee shall comprise at least three members. All members of the Committee shall be independent non-executive Directors of the Company appointed by the Board, on the recommendation of the Nominations Committee in consultation with the Chairman of the Committee, in accordance with the Company's articles of association.
- The Committee as a whole shall have competence relevant to regulated and/or utilities businesses and at least one member of the Committee shall have significant recent and relevant financial experience. Such individuals will have no higher degree of individual responsibility or obligation than other members. The Chairman of the Board shall not be a member of the Committee.
- Only members of the Committee have the right to attend Committee meetings. The Chief Financial Officer, external Auditor and Head of Internal Audit will be expected to attend meetings of the Committee on a regular basis. The Chairman of the Board, Chief Executive and other Directors and representatives from the Company may be invited to attend all or part of any meeting as and when appropriate and necessary.
- Appointments to the Committee shall be for an initial period of three years. The period of office may be extended for such duration as may be determined by the Board, so as long as the member continues to be an independent non-executive Director.

- The Board shall appoint one of the Committee members to be the Committee Chairman on the recommendation of the Nominations Committee. 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.
- The Chairman and Committee members shall be listed on the Company's website and each year in the Company's Annual Report and Accounts.
- Any such member shall abstain from voting on resolutions and participating in the discussions concerning such resolutions.
- Each member of the Audit Committee shall disclose to the Committee:
 - A. Any personal financial interest (other than as a shareholder) in any matter to be decided by the Audit Committee; or
 - B. Any potential conflict of interest arising from a cross-Directorship or other business interests.

4. Secretary

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

5. Quorum

- The quorum necessary for the transaction of business by the Committee will be two members, one of whom should normally be the Chairman of the Committee or his or her appointed deputy.
- In the event that a meeting of the Committee is required but a quorum might not be secured, an existing member of the Committee shall be empowered, to appoint another non-executive Director(s) to attend such meeting in consultation with the Chairman of the Committee to act as that member's alternate.

6. Frequency of Meetings

Meetings shall be held at least four times per year, and at any other time as the Committee's role and responsibilities require, and otherwise as the Chairman of the Committee shall require.

7. Notice of Meetings

- Meetings of the Committee shall be called by the Secretary of the Committee at the request of any of its members.

- 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 and any other person required to attend 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 to enable proper consideration of matters by the Committee.
- Members may participate in a meeting by means of telephone, video conferencing facility or other suitable communication equipment.

8. Minutes of Meetings

- The Secretary shall minute the proceedings and decisions of all meetings of the Committee, including recording the names of those present and in attendance and the existence of any conflicts of interest.
- Draft minutes of Committee meetings shall be circulated promptly to all members of the Committee after a meeting. Once approved, minutes should be circulated to all other members of the Board and attendees unless the Committee Chairman considers that it would be inappropriate to do so.

9. Annual General Meeting

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

10. Duties

The Committee should carry out the duties below in respect of Severn Trent Plc and its major operating subsidiaries.

(a) Financial Reporting

- The Committee shall monitor the integrity of the financial statements of the Company, including its annual and half-yearly reports, interim management statements, preliminary announcements and any other formal announcement relating to its financial performance and shall review and, where appropriate, report to the Board on significant financial reporting issues and significant estimates and judgments which they contain.
- The Committee will advise the Board if it is not satisfied with any aspect of the Company's proposed financial reporting. In particular, the Committee shall review and challenge where necessary:
 - A. significant accounting policies and practices, and any changes to them;

- B. whether the Company has followed appropriate accounting standards and made appropriate estimates and judgments;
- C. the methods used to account for significant or unusual transactions where different approaches are possible and the extent to which the financial statements are affected;
- D. the clarity, completeness and appropriateness of disclosures in the Company's financial reports and the context in which disclosures are made;
- E. any significant adjustments arising from the audit;
- F. related information presented with financial statements, including, without limitation, the going concern and viability statements to be made by the Board of the Company and the related information presented with the financial statements (including the Strategic Report and Corporate Governance statements relating to the audit);
- G. the risks to the quality and effectiveness of the financial reporting process; and
- H. the Company's disclosure controls and procedures, including reviewing reports of the Severn Trent Disclosure Committee.

The Committee will review the process undertaken to ensure that Directors are able to make the statement required by section 418 Companies Act 2006 in respect of relevant audit information. The Committee will review the process undertaken to ensure that Directors are able to make the statement required by Code Provision C1.1 that the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position, performance, business model and strategy.

(b) Regulatory Reporting

In respect of Severn Trent Water Limited and Dee Valley Water Limited, the Committee will review and challenge where necessary:

- the integrity of the processes that ensure the quality and reliability of the information within the Annual Regulatory Compliance Statement and Annual Performance Report, submitted to the Office of Water Services (Ofwat); and
- the integrity of the processes that ensure compliance with the requirements of the Scheme of Charges submitted to Ofwat, including the intentions and the rationale behind tariff proposals for the coming charging year and compliance with licence Condition E.

(c) Internal Controls and Risk Management

The Committee shall provide assurance to the Board that the Company's control assurance processes are implemented, complete and effective. In particular:

- keep under review the adequacy and effectiveness of the Company's internal controls and internal control and risk management systems;
- review and approve the statements to be included in the Severn Trent Plc Annual Report, prior to endorsement by the Board and external auditors, and the Annual Regulatory Compliance Statement concerning internal controls and risk management.

- review and challenge the policies and overall process for identifying and robustly assess business risks (financial and non-financial) and managing their impact on the Company;
- review regular reports from management, internal audit and external audit on matters related to risk and control; and
- review the timeliness and effectiveness of corrective action taken by management.

(d) Internal Audit

The Committee shall:

- monitor and review the effectiveness, independence and objectivity of the Company's internal audit function in the context of the Company's overall risk management system;
- approve the appointment and, as necessary, the removal of the Head of the internal audit function;
- consider and approve the remit of the internal audit function having regard to the complementary roles of the internal and external audit functions and ensure it has adequate resources and appropriate access to information to enable it to perform its function effectively and in accordance with the relevant professional standards. The Committee shall also ensure the function has adequate standing and is free from management or other restrictions;
- review and assess the annual internal audit plan, including any material changes to the audit plan;
- review reports addressed to the Committee from the internal auditor on a periodic basis;
- review and monitor management's responsiveness in remedying internal audit's findings and recommendations and any deficiencies identified by supervisory bodies related to the internal audit function;
- meet the Head of internal audit at least once a year, without management being present, to discuss their remit and any issues arising from the internal audits carried out; and
- ensure that the Head of internal audit has the right of direct access to the Board and to the Committee Chairman and is accountable to the Committee.

(e) External Audit

The Committee shall consider matters relating to the appointment of the external auditor, including:

- making 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 Company's external auditor;
- making recommendations to the Board that the external audit is put out to tender at least as often as is required by applicable law, rules, regulations and best practice, and, if the Committee believes that the applicable timetable should not be complied with, seeking approval of the Board to non-compliance;
- 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 and transparency report;

- if the Committee decides to consider the appointment of a new auditor, initiate and oversee a fair tendering and selection process, and, if the auditor resigns, investigate the issues leading to this and decide whether any action is required;
 - overseeing the relationship with the external auditor including (but not limited to):
 - A. approval of their remuneration for audit and non-audit services, including establishing whether the level of fees is appropriate to enable an adequate audit to be conducted;
 - B. developing and implementing a policy on the engagement of the external auditor to supply non-audit services by the external auditor to avoid any threat to auditor objectivity and independence, taking into account the regulations and ethical guidance on the matter and reporting to the board on any improvement or action required;
 - C. approval of their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;
 - D. assessing their independence and objectivity taking into account relevant law, regulations and professional requirements, the relationship with the auditor as a whole, including the provision of any non-audit services;
 - E. satisfying itself that there are no relationships (such as family, employment, investment, financial or business) between the auditor and the Company (other than in the ordinary course of business);
 - F. agreeing with the Board a policy on the employment of former employees of the Company's external auditor and monitoring the application of this policy;
 - G. monitoring the auditor's compliance with relevant ethical and professional requirements relating to, among other things, the rotation of audit partner, the level of fees paid by the Company compared to the overall fee income of the firm, office and partner and other regulatory requirements; and
 - H. seeking to ensure co-ordination with the activities of the internal audit function:
 - meeting 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 the auditor's remit and any issues arising from the audit;
 - reviewing and approving the annual audit plan and ensuring that it is consistent with the scope of the audit engagement;
 - reviewing the findings of the audit with the external auditor. This shall include but not be limited to, the following:
 - A. a discussion of any major issues which arose during the audit;
 - B. any accounting and audit judgments;
 - C. levels of errors identified during the audit; and
 - D. the effectiveness of the audit process.
 - E. reviewing any representation letter(s) requested by the external auditor before they are signed by management; and
 - F. reviewing the management letter and management's responsiveness in remedying the external auditor's findings and recommendations.
- (f) Whistleblowing

The Committee shall consider matters relating to Whistleblowing, including:

- overseeing the Group's whistleblowing policies and procedures, assessing their effectiveness and ensuring management provide an annual update on whistleblowing to the Board;
- receiving reports on whistleblowing matters, including material instances of disclosure, at every meeting of the Committee;
- ensuring that management has internal arrangements in place to handle any type of whistleblowing disclosure by any person, including anonymous disclosures;
- reviewing the adequacy and security of the Group's whistleblowing arrangements and ensuring that these arrangements allow effective assessment and escalation of concerns.
- overseeing the Company's processes, systems and controls for the prevention of bribery and receive reports on non-compliance.
- reviewing major findings of any relevant internal investigation into control weaknesses, fraud or misconduct, and management's response to this (in the absence of management where necessary); and
- consideration of whether any public disclosures are needed where there have been issues with internal control procedures.

11. Reporting Responsibilities

- The Committee Chairman shall report orally to the Board on its proceedings after each meeting on all matters within its duties and responsibilities and shall also report on 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;
- The Committee shall approve the section in the Annual Report which deals with the activities of the Committee and shall formally report such to the Board and;
- If the external auditor provides non-audit services, to provide an explanation for inclusion in the Annual Report and Accounts of how auditor objectivity and independence is safeguarded.

12. Other Matters

The Committee shall:

- have access to sufficient resources in order to carry out its duties, including access to the company secretariat for assistance as required;

- 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;
- give due consideration to laws and regulations, the provisions of the Code and the requirements of the UK Listing Authority's Listing, Prospectus and Disclosure and Transparency Rules, Disclosure Guidance and any other applicable rules, as appropriate;
- be responsible for co-ordination of the internal and external auditors;
- oversee any investigation of activities which are within its terms of reference; and
- arrange for periodic reviews of its own performance and, at least annually, review its 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.

13. Authority

The Committee is authorised:

- to seek any information it requires from any employee of the Company in order to perform its duties;
- to obtain, at the Company's expense, outside legal or other professional advice on any matter within its terms of reference. In this regard any Board policy document concerning the securing of such advice shall be adhered to by the Committee:
 - A. the Committee is exclusively responsible for establishing the selection criteria for such advisors and their appointment and terms of reference; and
 - B. the appointment and performance of such advisors shall be reviewed by the Committee on a regular basis and at least annually;
- to call any employee to be questioned at a meeting of the Committee as and when required; and
- to have the right to publish in the Company's Annual Report details of any issues that cannot be resolved between the Committee and the **Board**.