

**NORTHUMBRIAN WATER GROUP PLC**  
**THE AUDIT COMMITTEE**  
**TERMS OF REFERENCE**

References to “the Committee” in these Audit Committee Terms of Reference shall mean the Audit Committee of Northumbrian Water Group plc.

References to “the Board” shall mean the Board of Directors of Northumbrian Water Group plc.

References to “NWG” or the “Company” shall mean Northumbrian Water Group plc

References to “Group” shall mean the Company and its subsidiaries.

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1. The purpose of the Committee is to assist both executive and non-executive directors of NWG to discharge their individual and collective responsibilities in relation to:
    - (i) ensuring the financial and accounting systems of NWG and its subsidiaries are providing accurate and up-to-date information on its current position;
    - (ii) ensuring NWG’s published financial statements represent a true and fair reflection of this position; and
    - (iii) assessing the scope and effectiveness of the Group’s risk management systems and the integrity of its internal financial controls.
  
  2. Membership and Attendance
    - (i) The Committee shall be appointed by the Board, on the recommendation of the Nomination Committee and in consultation with the Audit Committee Chairman, and shall comprise of at least three members.
    - (ii) All members of the Committee shall be independent non-executive directors of NWG. The Chairman of the Board shall not be a member of the Committee. At least one member of the Committee shall have recent relevant financial experience.
    - (iii) The Committee shall ensure that the risk of any conflict of interest that might be seen to give rise to an unacceptable influence is minimised.
    - (iv) The Board, on the recommendation of the Nomination Committee, 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 their number present to chair the meeting.

- (v) The Committee may ask the Chairman, Managing Director, Finance Director and any relevant senior managers to attend meetings either regularly or by invitation, but the invitees have no right of attendance.
- (vi) The Committee shall normally ask a representative of the external auditors and the Internal Audit Manager to attend meetings. The Committee shall have at least one meeting a year, or part thereof, with the external and internal auditors without management being present.

### 3. Secretary

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

### 4. Quorum

The quorum necessary for the transaction of business shall be two. 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. Frequency of Meetings

- (i) The Committee shall meet not less than three times a year and at such other times as the Chairman of the Committee shall require.
- (ii) Meetings will be arranged to tie in with the publication of the Company's financial statements.
- (iii) Meetings can be requested by the external or internal auditors if they consider it necessary.

### 6. Notice of Meetings

- (i) Meetings of the Committee shall be called by the Secretary of the Committee.
- (ii) Unless otherwise agreed, notice of each meeting confirming the venue, time and date together with an agenda of items to be discussed and supporting papers (where relevant), shall be forwarded to each member of the Committee and any other person required to attend, no fewer than 5 working days prior to the date of the meeting.

### 7. Reports and Minutes of Meetings

- (i) The Chairman of the Committee will report to the Board the main items of business addressed at each meeting of the Committee.

- (ii) The Secretary shall minute the proceedings and resolutions of all meetings of the Committee, including recording the names of those present and in attendance.
- (iii) The Secretary shall ascertain, at the beginning of each meeting, the existence of any conflicts of interest and minute them accordingly.
- (iv) Minutes of Committee meetings shall be circulated to all members of the Committee and to the Chairman and all members of the Board.

## 8. 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.

## 9. Duties

### (i) Internal Control and Risk Assessment

The Committee shall review:

- the effectiveness of the Company's financial reporting and internal control policies and procedures for the identification, assessment and reporting of risks; and
- the Company's statement on internal control systems prior to endorsement by or on behalf of the Board, having reviewed the policies and process for identifying and assessing business risks and the management of those risks by the Company.

### (ii) Internal Audit

(a) The Committee shall review:

- applications for the post of Internal Audit Manager (and shall approve such appointment) and any proposal to dismiss the post holder;
- (and approve) the Internal Audit Charter and shall be advised of the planned programme of internal audits and the reason for any change or delay in the programme;
- the effectiveness of the internal audit function and update, as necessary, the mission and scope of work of the internal audit function, as contained in the Internal Audit Charter;
- the management of financial matters and focus upon the freedom allowed to the internal auditors;
- all reports on the Company from the internal auditors;

- the resourcing of internal audit function and its standing within the Company;
  - the self-certification reports on internal financial controls from operating subsidiaries ; and
  - the Company's statement on internal financial control systems prior to endorsement by the Board.
- (b) The Internal Audit Manager shall have the right of direct access to the Chairman of the Committee and the Committee shall meet with the Head of Internal Audit at least once a year without the presence of management.
- (iii) External Audit
- (a) The Committee shall consider and make recommendations to the Board as regards the appointment, re-appointment, resignation and/or dismissal of the Company's external auditors, and shall ensure that audit partners are rotated in accordance with applicable United Kingdom ethical guidance relating to the rotation of audit partners.
- (b) The Committee shall meet with the external auditors at least twice each year, once at the planning stage, to consider the scope of the audit, and once post audit at the reporting stage, to review the effectiveness of the audit process at the end of the annual audit cycle, and shall ensure that any audit representation letters, auditor's management letters and management's responses are reviewed.
- (c) The Committee shall keep under review the relationship with external auditors including (but not limited to):
- the independence, objectivity, effectiveness, qualifications, expertise and resources of the external auditors;
  - the consideration of audit fees as well as any other fees which are payable to auditors in respect of non-audit activities;
  - developing and implementing policy on the engagement of the external auditor to supply non-audit services and monitoring the provision and scope of any such services; and
  - discussions with the external auditors concerning such issues as compliance with accounting standards and any proposals which the external auditors have made regarding the Company's internal auditing standards.

(d) The Committee shall consider all significant problems and reservations arising from the interim and final audits and any matters the external auditor may wish to discuss (in the absence of management where appropriate).

(iv) Financial Statements

(a) The Committee shall keep under review the consistency of accounting policies both on a year to year basis and across the Company and Group.

(b) The Committee shall review and challenge where necessary the Company's interim management statements and half-year and annual financial statements taking into account:

- decisions requiring significant judgement;
- the extent to which the financial statements are affected by any unusual transactions;
- the clarity and completeness of disclosures;
- significant adjustments resulting from the audit;
- the going concern assumption;
- compliance with accounting standards; and
- compliance with stock exchange and other requirements.

(v) Reporting Responsibilities

(a) The Committee shall review the Annual Report and at least once a year shall review the relationship with the internal and external auditors.

(b) The Committee shall make whatever recommendations to the Board it deems appropriate and shall compile a report to shareholders to be included in the Company's Annual Report and Accounts.

(c) The Committee shall monitor the integrity of any formal announcements relating to the Company's financial performance, reviewing significant financial reporting judgements contained in them.

(vi) Other Matters

The Committee shall:

- give due consideration to the requirements of the UK Listing Authority's Listing Rules and relevant laws, regulations, accounting standards and best practice guidelines from time to time in force;
- co-ordinate the internal and external auditors;
- review the Company's procedures for handling allegations from whistleblowers and report any such allegations to the Board;
- oversee any investigation of activities, which are within its terms of reference and act as a forum of last resort;
- regularly review its own performance, constitution and terms of reference to ensure it is operating at maximum effectiveness; and
- ensure its members are trained and kept up to date in matters such as the regulatory framework of the Group, the main principles of and developments in financial reporting and related company law and the role of internal and external auditing and risk management.

#### 10. Authority

The Committee is authorised:

- to instigate an investigation into any matter within its terms of reference;
- 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 matters within its terms of reference; and
- to call any member of staff to be questioned at a meeting of the Committee as and when required.