



**HFC LIMITED**

**AUDIT COMMITTEE - TERMS OF REFERENCE**

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**1. OBJECTIVE**

To provide independent oversight of the institution's financial reporting and internal control system, ensure checks and balances within the institution are in place and to recommend appropriate remedial action regularly, preferably at least once in three months. In a group structure, the board of directors and senior management of the parent institution have the overall responsibility for ensuring that an adequate and effective internal audit function is established across the group and for ensuring that internal audit policies and mechanisms are appropriate to the structure, business activities and risks of all the components of the group.

**2. APPOINTMENT AND MEMBERSHIP**

**2.1** The Audit Committee (AC) will be appointed by the Board. The AC membership will not comprise members who are executive directors, or are involved in the management, or are officers of the company. The number of members shall be determined by the Board from time to time (It is recommended that the membership should not exceed five members).

The Chairman of the board should neither be the chairperson nor member of the AC but may be invited to attend meetings as necessary by the Chairman of the Committee.

The AC shall comprise of at least three non-executive members of the Board, with a majority being independent.

**2.2** When making the appointment the Board will ensure that:

- Every member appointed is independent of current management or has not been involved in the management of the institution in the last two years preceding his appointment, and is free from any relationship that in the opinion of the Board would interfere with his exercise of independent judgment.
- At least one of the members has a background in finance and audit.
- Every member appointed is familiar with the AC's terms of reference.
- Every member appointed is aware of the interest of all stakeholders.

**2.3** The Board will have the absolute power to appoint and remove any member of the AC, and to fill all casual vacancies that may arise.

**2.4** AC will be chaired by one of the non-executive directors who shall be appointed by the Board from amongst the AC members.

- 2.5** The term of the office of the AC members shall be fixed by the Board and shall be tied to their term of office as directors.

The Board will periodically review the composition of the AC and make any changes it deems appropriate.

- 2.6** The following, who shall have no voting rights, may attend the meetings of the AC on invitation from the AC:
- The institution's Chief Executive Officer/ Managing Director.
  - The Head of the Internal Audit Division
  - The external auditors.
  - Representative of the Central Bank of Kenya.
  - Any other person at the discretion of the AC.

### **3. POWERS AND DUTIES AS CONFERRED UPON THE COMMITTEE BY THE BOARD**

- 3.1** AC will have explicit authority to investigate any matters within its terms of reference.

The Board may delegate tasks or duties to the AC and require that the AC carries out such tasks with or without reporting back to the Board.

The (AC) should play a key role in ensuring that the Company's internal audit function is independent and has the necessary resources; budget, standing and authority to enable it discharge its functions effectively.

- 3.2** The principal role of the AC will be to assist the Board in raising the standards of corporate governance in the following areas:
- Improving the quality of financial reporting by ensuring that the accounts are prepared in a timely and accurate manner to facilitate prompt publication of annual accounts;
  - Strengthening the effectiveness of the internal and external auditing functions by ensuring the establishment of a permanent internal audit function. In fulfilling its duties and responsibilities, the board and senior management should take all the necessary measures to ensure that the institution has a permanent internal audit function commensurate with its size, nature and complexity of its operations ;
  - Reviewing and monitoring the external auditors' independence and objectivity, taking into consideration relevant professional and regulatory requirements. In fulfilling its duties, the AC will review with the external auditors, the scope of their audit plan, system of internal audit reports, assistance given by management and its staff to the auditors and any findings and actions to be taken.

- Strengthening the control environment;
- Increasing the stakeholders confidence in the credibility and stability of the Company; and
- Monitoring instances of non-compliance with Central Bank of Kenya Act, Banking Act, Central Bank of Kenya Prudential Regulations and other legislation, and advising the Board, on best practice.

In carrying its duties the AC:

- Will have access to resources of the company and the reports and working papers of the Internal Audit Division (IAD), and full access to any information and documentation of the company.
- Can obtain professionals advice and if necessary invite professionals with relevant experience to attend the AC's meetings, or to carry out such work as deemed necessary. Any expenses incurred shall be borne by the Company upon prior approval of the Board's chairman.
- May invite any director of the Company, or any other Staff member or a person connected directly or indirectly with the Company to assist with, and participate in the activities of AC.
- The management will circulate to the AC all correspondence received from the internal and external auditors and Central Bank of Kenya.

**3.3** The Internal Audit function shall report to the AC.

#### **4. REPORTING LINES AND MEETING PROCEDURES**

- 4.1** The AC will report directly to the Board through the AC chairman.
- 4.2** The AC will appoint a secretary for the purpose of taking minutes of its meeting
- 4.3** Members of AC shall meet at least quarterly or more frequently as required.
- 4.4** The quorum at all meetings shall be two members. No member is permitted to appoint a proxy.
- 4.5** AC decisions shall be taken by a majority of votes of those present. In case of a tie, the Chairman shall have a second or casting vote.

The Chairman shall at his sole discretion and as he deems appropriate use the casting vote, or refer the matter to the full Board for decision.

- 4.6** The agenda and the discussion papers of the meeting shall be circulated to the members of AC, and those invited to the meeting at least one week prior to the next scheduled meeting.

The minutes of the meeting and the action plan arising therefrom shall be circulated to the Board chairman, members of AC, and those who attended the meeting within two weeks of the meeting.

- 4.7** The report of the AC will form a regular feature on the Board's agenda. The report shall include the scheduled audit plans, summary of key audit issues and actions taken to date, the minutes of the AC, and any other issues that require Board input.

## **5. DUTIES AND RESPONSIBILITIES**

In carrying out the duties conferred upon the AC in 3 above, the AC will have the following specific duties and responsibilities:

### **5.1 EXTERNAL AUDIT**

**5.1.1** On instructions from the Board to appoint external auditors, the AC will recommend to the Board the external auditors to be appointed after considering the scope of work, the audit fees, the profile and independence of the audit firms.

**5.1.2** The AC will hold open lines of communication with the external auditors prior to, during and post audit to cover the following:-

➤ Audit planning meeting to discuss:

- The annual audit timetable;
- The scope of work;
- The approach to work;
- Areas of management concern; and .
- Audit fees.

➤ Audit finalization meeting to discuss:

- Results of the annual audit;
- Any unresolved audit issues;
- Management letter, setting up a timetable for implementation by the management;
- Adequacy of the financial policies and procedures;  
and

- Review of the financial statements and whether they constitute a full and meaningful report to all stakeholders to include:
  - Any changes in accounting policies and practices;
  - Major judgmental areas;
  - Significant adjustments resulting from audit; -
  - The going concern assumption;
  - Compliance with accounting standards and legal requirements; and
  - Compliance with any other regulatory requirements including the Central Bank of Kenya Act, Banking Act, and Central Bank of Kenya Prudential Regulations and Circulars issued by the Central Bank of Kenya.
- Ensuring that the management does not restrict the audit scope.

**5.1.3** Review all significant issues concerning litigation, contingencies, claims or assessments and all material accounting issues that require disclosure in the financial statements. This review should include a discussion of recent Central Bank of Kenya pronouncements that have a material impact on the Company.

**5.1.4** Monitor instances where management seeks a second opinion on significant accounting matters.

**5.1.5** Review of taxation affairs and status of the company.

## **5.2 INTERNAL AUDIT**

**5.2.1** Evaluate and shortlist the candidate for the position of the Head of IAD and recommend to the Board the ideal candidate for the position.

**5.2.2** Review the scope and the effectiveness of the IAD and provide direction on enhancing the utility of the IAD through clearly laid down processes, procedures and time frames.

This will include:-

- Review of the internal audit programmes, their objectives and the Staff level required to attain these objectives.
- Review of the internal audit reports and implementation of the same based on set timeframes.
- Providing input on the internal audit reports to management and highlighting areas of concern to and/or requiring guidance from the Board.
- Establishing working relationships between the IAD and the external auditors and strengthening the position of the internal audit function in providing it with a greater degree of independence from management.

- 5.2.3 Evaluate staff engaged in the internal audit function in consultation with the chairman of the Board, and review and approve the proposed remuneration of the staff of the IAD including annual increments and performance bonuses.
- 5.2.4 Review the division's and individual's terms of reference and proposing to the Board any amendments thereto.
- 5.2.5 Commission such ad-hoc internal audit assignments as deemed necessary by AC, management or the Board.
- 5.2.6 Ensure implementation of all relevant policies and procedures approved by the Board, as well as of the various guidelines and instructions of the Board.

### **5.3 CENTRAL BANK OF KENYA**

The AC will provide a linkage between the Board and the Central Bank of Kenya in the following areas:

- Attending the tripartite meetings between the Company, the external auditors and the Central Bank of Kenya.
- Review the Central Bank of Kenya inspection report prior to presentation of the same to a full Board and providing comments and developing an implementation plan for the same.
- Review the Central Bank of Kenya circulars and pronouncements and to ensure that the Company complies with the same.
- Holding discussions with the Central Bank of Kenya on any area of concern and discussing the bank implementation plan on the same.

### **5.4 FINANCIAL AND RELATED ISSUES**

- 5.4.1 Monitor and provide direction on the review and development of the Company's policies and procedures to include:
  - The Company's code of conduct for directors and employees which creates a climate of discipline and control, and which in turn reduces the opportunity for fraud.
  - Financial, operating, human resource and corporate governance policies, and ensuring that the financial resources are invested prudently providing an optimum return.

- Policy on management of key banking risks of credit, liquidity, interests currency, off balance sheet, system failure and position risks.

**5.4.2** Review the management information and reporting systems, as well as the timetable for the submission of reports, and to recommend appropriate formats and time frame for submission of these reports. The key reports would include:

- Financial performance and budget variance reports-
- Report non-performing assets.
- Concentration of assets / liabilities.
- Assessment of key banking risks of credit, liquidity, interests, currency, off balance sheet, systems failure and position risk.
- Non compliance.

**5.4.3** Oversee that the Company's internal control are operating as per the laid down policies and procedures, and providing direction for strengthening the internal control environment.

**5.4.4** Review the electronic data processing environment to ensure that it is protected against risks such as system failure, data security and physical security.

**5.4.5** Provide input to the annual budget and business plan development and review process.

**5.4.6** Monitor the status of non-performing advances and recommend the adequacy of bad debt provisions.

**5.4.7** Monitor the level of capital adequacy and keeping the Board informed on the same.

**5.4.8** Keep the Board informed on any significant developments in the accounting and disclosure requirements, reporting requirements and other such related issues.

## **5.5 OTHERS**

**5.5.1** Review the AC's terms of reference at least once every three years and recommend modifications.

**5.5.2** Carry out other tasks, special assignments and investigations as may be requested from time to time by the Board or the management.

**5.5.3** Consider any matter of significance raised at the risk management committee meetings.

- 5.5.4 Review any related party transactions that may arise within the banking institution.
- 5.5.5 Monitor the ethical conduct of the institution and consider the development of ethical standards and requirements, including effectiveness of procedures for handling and reporting complaints
- 5.5.6 Review compliance to financial and related directives issued by the Kenya Revenue Authority, the Central Bank of Kenya, the Institute of Certified Public Accountants of Kenya and compliance with legislation including the Central Bank of Kenya Act, Banking Act and the Companies Act.

**APPROVED BY THE HFC BOARD 19<sup>TH</sup> APRIL 2018**