



**CHARTER OF THE AUDIT COMMITTEE
OF THE MANAGEMENT BODY**

DECEMBER 2016

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AUDIT COMMITTEE CHARTER

1. AUDIT COMMITTEE CHARTER

This Charter establishes the role and terms of reference of the Audit Committee within the Cyprus Development Bank and its subsidiary companies (CDB Group). The Charter will be approved by the Management Body and may be revised from time to time to adapt to the needs of the CDB Group as they emerge and to comply with the requirements of the Central Bank of Cyprus.

2. MISSION OF THE AUDIT COMMITTEE

The mission of the Audit Committee is to assist the Management Body in fulfilling their oversight responsibilities in relation to:

- the internal and external audit processes;
- the Group's system of internal control and management of financial and operational risks;
- the quality and integrity of the Group financial statements and the financial reporting process; and
- the Group's compliance with legal and regulatory requirements.

3. REQUIREMENTS TO ESTABLISH THE AUDIT COMMITTEE

The Bank must establish management body committees that are appropriate to the size, internal organisation and the nature, scope and complexity of their activities.

It is provided that Banks must also establish an audit committee referred to in Section 46 of the Auditors and Statutory Audits of Annual and Consolidated Accounts Law of 2009.

The Central Bank may allow the Bank which is not considered significant in terms of its size, internal organisation and nature, scope and complexity of its activities to combine the risk committee with the audit committee and / or the nomination committee with the remuneration committee; members of a combined committee shall have the knowledge, skills and expertise required for the committees is composed of.

Banks must communicate the composition of management body committees to the Central Bank within one (1) month of their set up or of change of the composition.

4. COMPOSITION OF THE AUDIT COMMITTEE

The Audit Committee shall comply with the following regarding its composition:

- The number of members of committee must be sufficient, and in all cases not less than three (3) members, to handle the size and complexity of its functions;
- More than fifty percent (50%), of the committee members must be independent members.

- The committee shall be composed of Members of the Management Body who do not perform any executive function in the Bank.
- Committee Members must not hold any other posts or positions or conduct transactions which could be considered to be in conflict with the terms of reference of the committee.
- Cross committee membership must ensure that no individual exercises excessive influence or control; a member of the Management Body must not be a member of more than two of the following committees: (i) Audit Committee, (ii) Risk Committee and (iii) Nomination Committee and Remuneration Committee.

The Committee must report regularly to the Management Body and it must circulate its minutes to the Management Body in advance of Management Body meetings.

The Management Body must establish a process for the co-ordination and communication among its different committees.

The Bank must ensure that the Committee has adequate access to the Internal Audit Function and Compliance Function and to external expert advice and that the Heads of the respective control functions are invited regularly in the meetings of the Committee.

The Chairperson of the Committee must ensure that no other person is present, including other members of the Management Body, unless formally invited to attend for a specific item on the agenda; any such person is present only during the discussion of the specific item and leaves the meeting room immediately after, without any participation in the decision making process.

5. AUDIT COMMITTEE MEMBERSHIP ELIGIBILITY CRITERIA

Based on the *Directive of Governance and Management Arrangements in Credit Institutions (July 2014)* the Audit Committee membership eligibility criteria are the following:

- The Audit Committee as a whole should have:
 - recent and relevant practical experience in the area of financial markets or professional experience directly linked to financial markets activity;
 - knowledge of the Bank's broader business environment including information systems and technology.
- The Chairperson of the Audit Committee must be independent and have specialist knowledge and experience in the application of accounting principles and internal control processes.
- The Chairperson of the Management Body may not be a member of the audit committee.
- Audit Committee meetings, where appropriate, must coincide with important financial reporting dates.

6. AUTHORITIES

The Management Body authorises the Audit Committee to conduct or authorise investigations into any matters within its scope of responsibility. It is empowered to:

- seek any information it requires from employees - all of whom are directed to co-operate with the Committee's requests - or external parties;
- retain independent counsel, accountants, or others to advise the Committee or assist in the conduct of an investigation;
- resolve any disagreements between management and the auditors; and
- meet with Group officers, external auditors, or outside counsel, as necessary.

7. ORGANISATION

7.1 Appointment

The Management Body shall appoint the Audit Committee and this appointment shall remain effective until the expiry of their term of office. The Audit Committee Chairman shall be appointed by the Management Body. The Chairman of the Audit Committee should possess the necessary knowledge and expertise for the supervision of the auditing procedures and accounting matters which are of concern to the Committee.

The membership of the Committee shall consist of at least three members. The Audit Committee, as a whole, should possess appropriate knowledge and expertise, including knowledge of the bank's broader business environment including information systems and technology.

Each member shall be free of any relationship that, in the opinion of the Management Body, would interfere with his or her individual exercise of independent judgement.

The Secretary of the Audit Committee will be the Secretary of the Management Body. The Secretary may delegate her tasks to a third person provided that there is no conflict of interest and the Secretary checks and signs paperwork and remains responsible and accountable for the outcomes of the delegation. It is clarified that the Secretary may not delegate her tasks to the Heads of the Internal Audit or Compliance.

7.2 Attendance at meetings

The Audit Committee shall meet at least quarterly, with authority to convene additional meetings, as circumstances require. The Audit Committee's Chairman is responsible for informing the Management Body for the work performed by the Committee.

A quorum for any meeting will be two (2) members. All Committee members are expected to attend each meeting in person.

The Committee may invite members of management, internal and external auditors or others to attend meetings and provide pertinent information, as necessary. It may also hold private meetings with auditors and executive sessions on an ad-hoc basis.

Meeting agendas will be prepared and provided in advance to Members, along with appropriate briefing materials. The agendas will be prepared by either the Internal Auditor or the Compliance Officer, depending on issues to be included in the Agendas. Minutes shall be kept by the Secretary for the proceedings of the meetings.

8. RESPONSIBILITIES

The main tasks of the Audit Committee shall be the following:

- (a) the monitoring and assessment, on an annual basis, of the adequacy and effectiveness of internal control and information systems, based on reports from the internal audit function and the observations and comments of external auditors and competent supervisory authorities and subsequently the submission of proposals to the Management Body for addressing any weaknesses which have been identified;
- (b) the submission of proposals to the Management Body on the appointment, compensation, terms of engagement and substitution or rotation of the approved auditor and other external auditors;
- (c) the liaison with external auditors particularly in relation to their audit findings;
- (d) the assessment and monitoring of the independence, adequacy and effectiveness of the internal audit function;
- (e) advising the Management Body, drawing on the work of the compliance function, on the adequacy and effectiveness of the framework for business conduct;
- (f) advising the Management Body, drawing on the work of the compliance function and external auditors, on the adequacy and effectiveness of the compliance framework;
- (g) the assessment and monitoring of the independence, adequacy and effectiveness of the compliance function or in the case where the tasks of the compliance function are carried out by a combined control function in accordance with paragraph 76(1) of the *Directive of Governance and Management Arrangements in Credit Institutions (July 2014)*, the assessment and monitoring of the independence, adequacy and effectiveness of the combined control function in carrying out the tasks of the compliance function;
- (h) the submission to the Management Body of recommendations for the appointment or removal of the head of the internal audit function and compliance function;
- (i) the annual appraisal of the heads of the internal audit function and compliance function and subsequently their submission to the Management Body;
- (j) the review and approval of the annual audit plan of the internal audit function and the compliance programme of the compliance function,

- (k) the review and approval of the budgets of the internal audit function and compliance function, ensuring that they are sufficiently flexible to adapt to variations in response to developments;
- (l) the oversight that senior management takes the necessary corrective actions in a timely manner to address control weaknesses, non-compliance with policies, laws and regulations and other weaknesses identified by external auditors, the internal audit and compliance functions and supervisory authorities;
- (m) the monitoring of the establishment of accounting policies and practices;
- (n) the monitoring of the financial reporting process and the integrity, accuracy and reliability of the Bank's financial statements and any formal announcements relating to the Bank's financial performance;
- (o) the carrying out of self-assessment and reporting its conclusions and recommendations for improvements and changes to the Management Body.

More specifically, the Audit Committee shall:

8.1 Financial Reporting – General

- gain an understanding of the current areas of greater financial and operating risk and how management is addressing these;
- consider with the internal and external auditors any fraud, illegal acts, deficiencies in internal controls or similar issues;
- review any legal matters which could significantly impact the financial statements; and
- review significant accounting and reporting issues and recent professional and regulatory pronouncements, and understand their impact on the financial statements.

8.2 Financial Reporting – annual financial statements

- review the annual financial statements, and consider whether they are complete, consistent with information known to Committee members and reflect appropriate accounting principles;
- focus on judgmental areas, provisions, litigation reserves, other financial commitments and contingencies;
- review with management and the external auditors the results of the audit, including any difficulties encountered; and
- review other sections of the annual report before its release and consider whether the information is consistent with members' knowledge about the Group and its operations.

8.3 Internal Control

- consider the effectiveness of the Group's internal control systems, including information technology security and contingency planning; and
- understand the scope of internal and external auditors' review of internal controls and procedures and review reports on significant findings and recommendations, together with management's responses.
- to assign at least once every three years the assessment of the adequacy of its internal control systems to external auditors, preferably a firm other than the Bank's current external auditors. The said assessment should be conducted on a consolidated group as well as on an individual company basis and the report prepared should also be submitted to the Central Bank of Cyprus. The above external auditors should be rotated after two consecutive assessments.

8.4 Internal Audit

- review the Internal Audit charter, plans, activities, staffing and organisational structure, and deal with the administrative and personnel matters of the Internal Audit function and ensure no unwarranted restrictions or limitations are made;
- review the performance of Internal Audit personnel and grant final approval in the appointment or replacement of the Internal Auditor;
- review the effectiveness of the Internal Audit function;
- ensure that significant findings and recommendations made by Internal Audit are received and discussed with the Internal Auditor on a timely basis;
- ensure that management responds to recommendations made by Internal Audit;
- monitor the implementation by management of internal audit recommendations; and
- meet separately with Internal Audit to discuss any matters that the Committee or the Internal Auditor believe should be discussed privately.

8.5 External Audit

- review the external auditors' proposed audit scope and approach, including co-ordination of audit effort with Internal Audit;
- review the performance of the external auditors, the audit fees and submit proposals to the Management Body on the compensation, terms of engagement and appointment or replacement of the auditors;
- evaluate the objectivity and independence of the external auditors, monitoring the nature and extent of any non-audit services provided, and discussing any business or other relationships with the auditors;
- ensure that significant findings and recommendations made by the external auditors are received and discussed with the external auditors on a timely basis;

- ensure that management responds to recommendations made by the external auditors;
- monitor the implementation by management of external audit recommendations; and
- meet separately with the external auditors to discuss any matters that the Committee or auditors believe should be discussed privately.

8.6 Compliance Function

- review the effectiveness of the Bank's Compliance framework;
- review the compliance risks associated with the Bank's business activities and ensure that appropriate measures are being taken to deal with these risks;
- review breaches of the Bank's compliance policy and regulatory framework;
- review the Compliance charter, plans, activities, staffing and organisational structure, and deal with the administrative and personnel matters of the Compliance Function and ensure no unwarranted restrictions or limitations are made;
- ensure that significant findings and recommendations made by Compliance are received and discussed with the Compliance Officer on a timely basis;
- ensure that management responds to recommendations made by Compliance;
- ensure that the Bank complies with the Prevention and Suppression of Money Laundering Activities Law of 2007 and subsequent amendments and the CBC Directives and circulars for the prevention of money laundering and terrorist financing issued in accordance with article 59(4) of the said Law;
- ensure that there is an internal alert procedure in place to facilitate the confidential reporting by employees of concerns, shortcomings, or potential violations in respect of the Bank's policies, legal, regulatory or business obligations, or ethical considerations. The Audit Committee is also responsible for reviewing all reports made by employees.
- review the effectiveness of the internal control systems for monitoring compliance with laws and regulations and the results of management's investigation and follow-up (including disciplinary action) of any instances of non-compliance;
- obtain regular updates from management, the auditors and legal counsel regarding compliance matters;
- review the findings of any examinations by regulatory bodies;
- review any material fines or other disciplinary actions taken by supervisory authorities in respect of the Bank or any employee;
- review and propose the approval to the Management Body of the following reports: (i) Compliance Officer's Annual Report, (ii) Money Laundering Compliance Officer's Annual Report, and, (iii) Money Laundering Compliance Officer's Annual Report on the risks of money laundering and terrorist financing that the Bank is exposed to and the measures taken for their management and mitigation;

- meet separately with the Compliance Officer to discuss any matters that the Audit Committee or the Compliance Officer believe should be discussed privately.

8.7 Reporting Responsibilities

- prior to finalisation of the Group annual report and accounts, submit an advisory report to the Management Body discussing Committee review results with appropriate recommendations;
- on an annual basis (or as the Management Body may otherwise determine), report back to the Management Body on all other Committee activities, issues and findings with appropriate recommendations; and
- inform the Management Body of any matters which may come to the Committee's attention which may significantly impact the financial condition of affairs of the business.

8.8 Other Responsibilities

- review and assess the adequacy of the Audit Committee Charter annually, requesting Management Body approval for proposed changes, and ensure appropriate disclosure as may be required by law or regulation;
- review whether the transactions between the Group companies, Management Body members, senior executives, the external auditors and other advisors, were on an arms' length basis;
- provide an open avenue of Management Body;
- institute and oversee special investigations as needed;
- perform other activities related to this Charter as requested by the Management Body;
- confirm annually that all responsibilities outlined in this Charter have been carried out; and
- evaluate the Committee's performance on an annual basis.