

# HONG KONG EXCHANGES AND CLEARING LIMITED

## TERMS OF REFERENCE AND MODUS OPERANDI OF THE AUDIT COMMITTEE

### 1 Status

The Audit Committee (the “**Committee**”) is a sub-committee of the board (the “**Board**”) of the Hong Kong Exchanges and Clearing Limited (the “**Company**”) to which the Board has delegated consideration of the matters set out in paragraph 4 below.

### 2 Purpose

The Committee is to serve as a focal point for communication between other directors, the external auditor and the internal auditor as regards their duties relating to financial and other reporting, internal controls, external and internal audits and such other matters as the Board determines from time to time.

The Committee is to assist the Board in fulfilling its responsibilities by providing an independent review and supervision of financial reporting, by satisfying themselves as to the effectiveness of the internal controls of the Company and its subsidiaries, and as to the adequacy of the external and internal audits.

Matters to be considered by the Committee shall include, but not be limited to, the matters set out below in paragraph 4.

The Committee should liaise with The London Metal Exchange and the LME Clear Limited (together with the Company, the “**HKEX Group**”) to facilitate group-wide consolidated financial reporting as part of the HKEX Group.

The Committee will take into account HKEX Group reporting requirements and policies in reviewing the financial statements.

### 3 Administrative Structure

#### (a) Composition

The Committee will be composed of at least five individuals (excluding the secretary of the Committee). All Committee members shall be non-executive directors and a majority of whom shall be independent non-executive directors under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. The Committee shall have familiarity with the financial reporting principles and practices applied by the HKEX Group in preparing its financial statements.

The chairman and members of the Committee shall be appointed by the Board after considering the recommendations of the Nomination and Governance Committee. The chairman of the Committee shall be consulted on the appointment of other members of the Committee. The chairman of the Board shall not be a member of the Committee.

Only members of the Committee have a right to attend meetings; however other members of the Board or management may be invited to attend, as appropriate. External auditors will be invited to attend meetings on a regular basis.

(b) **Chairman**

The Board shall appoint one of the non-executive directors of the Company to be the chairman of the Committee. In the absence of the chairman and/or an appointed deputy at any meeting, the Committee will elect one of the members present to act as chairman.

The chairman of the Committee should attend the annual general meeting to answer shareholder questions on the Committee's activities.

(c) **Reporting Procedures and Frequency of Meetings**

- (i) Minutes will be taken for all meetings and kept by the secretary of the Committee and, when the Committee chairman deems appropriate, tabled at meetings of the Board. Draft and final versions of minutes of the meetings should be sent to all Committee members for their comment and records, within a reasonable time after the meeting. The chairman of the Committee will present an oral report to the Board on the activities and decisions of the Committee.
- (ii) The Committee shall meet at least four times per year at appropriate times in the reporting and audit cycle and otherwise as required. Meetings shall be summoned by the secretary of the Committee.
- (iii) Meetings can be convened at the request of the Committee chairman, members or the external or internal auditors.
- (iv) The Group Head of Internal Audit or their nominee shall be the secretary of the Committee. Committee meeting dates shall be agreed in advance affording adequate notice for maximum participation. Papers prepared for the Committee may be sent (by appropriate medium) between meeting dates and decisions or recommendations solicited and received between meetings, where necessary, to avoid delays in the decision-making processes.

- (v) The Committee chairman shall report regularly and formally to the Board, at the next meeting of the Board following a meeting of the Committee, on matters within its remit, and any suspected frauds and irregularities, failures of internal control or suspected infringements of laws, rules and regulations which come to its attention and are of sufficient importance to warrant the attention of the Board. At least annually, the Committee should present a report to the Board which addresses the work and findings of the Committee during the year.
- (vi) Where there is disagreement between the Committee and the Board, adequate time should be made available for discussion of the issue with a view to resolving the disagreement. Where any such disagreement cannot be resolved, the Committee has the right to report on the issue to the shareholder as part of the report on its activities.

(d) **Quorum**

Three members shall constitute a quorum.

Decisions shall be determined by simple majority and, in the event of a tie, the chairman of the Committee shall have the casting vote. Proceedings of meetings of the Committee shall be governed by the provisions of Article 105 of the Articles of Association of the Company.

## **4 Areas of Responsibility**

### **4.1 Financial Reporting and Internal Controls**

#### **4.1.1 Financial Reporting**

- (a) The Committee shall monitor the integrity of the financial statements of the HKEX Group, including its annual, interim, and quarterly reports and any other formal announcement relating to its financial performance. The Committee shall review and challenge where necessary:
  - (i) the consistency of, and any changes to, accounting policies and practices on a year on year basis and across the HKEX Group;
  - (ii) the methods used to account for significant or unusual transactions where different approaches are possible;
  - (iii) whether HKEX Group has followed appropriate accounting and auditing standards and made appropriate estimates and judgments, taking into account the views of the external auditors;

- (iv) the clarity of disclosure in the HKEX Group's financial reports and the context in which statements are made;
- (v) any significant financial reporting issues and judgments and all material information presented with the financial statements, such as significant adjustments resulting from the audit, and the going concern assumption and any qualifications; and
- (vi) any significant or unusual items that are, or may need to be, reflected in financial reports and accounts, and must give due consideration to any matters that have been raised by the staff responsible for the accounting and financial reporting function, compliance function or auditor (internal or external).

#### **4.1.2 Internal Controls**

The Committee shall:

- (i) monitor, and review with management, risk and compliance functions, external auditor and internal auditor, the adequacy and effectiveness of the Company's policies and procedures regarding internal controls (including financial, operational, IT, risk management, information security, outsourcing, legal, compliance and those controls designed to detect material fraud), and any statement concerning internal controls to be included in the annual accounts prior to endorsement by the Board; and
- (ii) discuss with management the scope and quality of systems of internal control and review annually that management has discharged its duty to have an effective internal control system including the adequacy of resources, qualifications and experience of staff of the accounting and financial reporting function, and their training programmes and budget.

#### **4.2 Anti-bribery and Anti-corruption and Whistleblowing**

The Committee shall:

- (a) review and approve HKEX Group's assessment of the corruption risks to which it is subject and the framework of controls put in place to mitigate those risks, including but not limited to the HKEX Group's policies on anti-bribery and anti-corruption, and risk management;

- (b) monitor and oversee compliance with the HKEX Group's anti-bribery and anti-corruption policies or guidelines, including reviewing these policies on an annual basis to ensure that they remain adequate for the purposes of the Prevention of Bribery Ordinance (Chapter 201 of the Laws of Hong Kong) and any other applicable legislation;
- (c) where appropriate, seek advice or information from the Chief Executive or any other person it deems necessary regarding HKEX Group's policies or guidelines on anti-bribery and anti-corruption or compliance with them;
- (d) report to the Board with such recommendations as the Committee may deem appropriate in relation to anti-bribery and anti-corruption;
- (e) review and approve HKEX Group Whistleblowing Policy annually and provide channels for its employees and third parties who deal with HKEX Group to raise concerns, in confidence, about matters subject to the HKEX Group Whistleblowing Policy such as possible improprieties in financial reporting, internal control or other matters related to the Company, with the Committee. The Committee shall ensure that proper arrangements are in place for fair and independent investigation of these matters and for appropriate follow-up action; and
- (f) review HKEX Group's findings and quarterly report summarising internal investigations and management's response into matters subject to the HKEX Group Whistleblowing Policy such as any concerns raised on suspected frauds or irregularities or failures of internal controls or infringements of laws, rules and regulations.

### **4.3 Internal Audit**

The Committee shall:

- (a) monitor and review annually the effectiveness of HKEX Group's internal audit function, in particular, ensure the adequacy of resources, staff qualifications and experience, training programmes and budget. Ensure co-ordination between the internal and external auditors and ensure that the internal audit function has appropriate standing within the Company and within the HKEX Group;
- (b) review and approve the annual internal audit plan and discuss with the internal auditor any significant findings and recommendations arising from the internal audit activities;
- (c) review and monitor management's responsiveness to the findings and recommendations of the internal auditors;

- (d) meet with the Group Head of Internal Audit
  - (i) at least once every year, to discuss their remit and any issues arising from the internal audits carried out. Management of HKEX Group shall not be present for such discussions; and
  - (ii) regularly throughout the year as the Group Head of Internal Audit shall require.
- (e) where consultants or internal group resources are engaged by management of HKEX Group to review particular aspects of HKEX Group's risk identification and/or risk management issues and/or internal control issues the Committee should have access to all such reports and presentations and if considered appropriate request that such consultant(s) present to the Committee;
- (f) approve the Internal Audit Charter and review its effectiveness on an annual basis;
- (g) approve decisions regarding the appointment, removal, and salary of the Group Head of Internal Audit; and
- (h) review the performance evaluation of the Group Head of Internal Audit.

#### **4.4 External Audit**

The Committee shall:

- (a) consider and make recommendations to the Board, in relation to the appointment, re-appointment and removal of the Company's external auditors, oversee the selection process for new auditors and investigate a resignation by the external auditors.
- (b) oversee all relationships with the external auditors including but not limited to:
  - (i) approval of their remuneration (to be negotiated by management), whether fees for audit or non-audit services and that the level of fees is appropriate to enable an adequate audit to be conducted and approval of their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;
  - (ii) assessing annually their independence and objectivity taking into account relevant professional and regulatory requirements and the relationship with the auditors as a whole;

- (iii) assessing annually their qualifications, expertise and resources and the effectiveness of the audit process which shall include a report from the external auditors on their own internal quality procedures. Discuss with the external auditor the nature and scope of the audit and reporting obligations;
  - (iv) seek from the external auditor, on an annual basis, information about policies and processes for maintaining independence and monitoring compliance with relevant requirements, including provision of non-audit services and requirements regarding rotation of audit partners and staff, the level of fees paid by the Company and the HKEX Group compared to the overall fee income of the firm, office and partner and other related requirements; and
  - (v) agree with the Board the policy relating to the hiring of employees or former employees of the external auditor and monitor the applications of such policy. The Committee will consider whether as a result of such hiring there has been any impairment of the auditor's judgment or independence in respect of an audit. A former partner of the existing external auditing firm should be prohibited from acting as a member of the Committee for a period of two years from the date of this person ceasing to be a partner of the firm or to have financial interest in the firm, whichever is later.
- (c) meet with the external auditors (it being noted that the external auditors may participate in such meetings by telephone):
- (i) at every meeting to discuss their remit and any issues arising from the audit. Management of HKEX Group shall not be present for such discussions; and
  - (ii) regularly throughout the year (including at the planning stage before the audit and at the reporting stage after the audit) as the external auditors shall require.
- (d) review and approve the annual external audit plan and ensure that it is consistent with the scope of the audit engagement;
- (e) review the findings of the external audit with the external auditors (if necessary in the absence of management), including but not limited to, the following:
- (i) a discussion of any major issues and recommendations which arose during the audit;
  - (ii) any accounting and audit judgments;

- (iii) levels of operational and financial errors identified during the audit; and
  - (iv) any disagreements with management which if not satisfactorily resolved would result in the issue of a modified report on the financial statements (i.e., a qualified, adverse or disclaimer of opinion in their report).
- (f) obtain comments of management regarding the responsiveness of the external auditor to the needs of the HKEX Group, and review the effectiveness of the audit;
  - (g) review any representation letter(s) requested by the external auditors before they are signed by management; and
  - (h) review the management letter and management's response to the external auditors' findings and recommendations, and ensure that the Board will provide a timely response to issues raised in the external auditor's management letter.

Notwithstanding the matters above listed as part of the Committee's authority, the Committee shall not have authority to approve any decision that could have a significant impact on the risk profile of the Company or the HKEX Group. Any such decision shall be referred to the Board for approval.

The engagement of HKEX Group's external auditor to perform non-audit services is in general prohibited except for tax-related services. If a compelling reason exists to engage the external auditors due to their unique expertise in a particular area, this matter shall be considered in accordance with the HKEX Group Policy on external auditors providing services and the prior approval of the Committee is required.

## 5 Other Matters

### (a) Authority and Duties

The Committee shall:

- (i) have access to sufficient resources and training in order to carry out its duties;
- (ii) give due consideration to all relevant laws and regulations, investigate any activity within its terms of reference;
- (iii) have access to members of management, legal counsel, and invite the attendance of outsiders with relevant experience and expertise at any meeting if necessary;



- (iv) undertake regular and thorough review to ensure that the Company is meeting the listing rules of The Stock Exchange of Hong Kong Limited and the legal requirements in relation to financial reporting;
- (v) 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; and
- (vi) produce an annual report on its activities.

In addition to the above, the Committee may investigate, discuss or review matters outside its terms of reference if required to do so by the Board.

(b) **Powers**

The Committee is authorised to:

- (i) have access to any information, record or reports it requires from any employee of the Company or its subsidiaries in order to perform its duties and all employees are directed to cooperate with the Committee, subject to the applicable laws and regulations;
- (ii) obtain, at the Company's expense, outside legal or other professional advice on any matter within its terms of reference; and
- (iii) call any employee of the Company or its subsidiaries to be questioned at a meeting of the Committee as and when required.

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