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19 December 1991

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**COMMITTEE ON THE FINANCIAL ASPECTS
OF CORPORATE GOVERNANCE**

Here is a copy of part of the Conference Board Research Report No 914, which I mentioned to you. It is in fact a 1988 not a 1990 document. It contains so much material that I think it ought to be mandatory reading for members of your committee before we go firm. Incidentally, I am not at all convinced by Andrew Hugh Smith's arguments because I feel it would be perfectly possible to define a break-point between plcs which should have audit committees and those which need not.

I promised to let you have some comments on the 100 Group paper with which we closed the meeting. These are as follows.

On the definition of corporate governance I suggest simply "Corporate governance is the system by which companies are run". The reason for this broad but simple formulation is not to exclude all the external elements such as the market or banks or advisers which do in practice affect immensely the way in which each national machine operates. The word "system" includes both formal and informal structures and relationships and is in my view appropriate for another reason, viz that what we are concerned with is indeed systemic inadequacy.

Turning now to the summary of recommendations in the paper on 3(ii), I would have added "so as to facilitate a better balance on the board. The critical feature is that the board should in practice be strong enough to stand up to the CEO when this is necessary."

My other amendment would be to Recommendation 5.43. An extra sentence might be added which suggested "It should however become a matter of regular practice that the chairman should make a public third quarter statement to confirm his previous statements or to shade them in whichever way then seemed desirable". The point about this is to face up to the issue we all duck, viz that chairmen ensure that the market is fed with information about changes in prospects, usually in a surreptitious way through analysts. This must be wrong in principle, however subtly it is done, because it means giving the recipient privileged information.

As Hugh said he would like a note of my suggestions, I am copying this letter to him.

Appendix C

Statements of Duties and Procedures of the & Audit Committee

The following audit committee charters or statements of function were among the most complete and explicit of those provided by cooperators in this report. Excerpts from many such statements are found throughout the body of the text.

An Energy Company

The board of directors hereby constitutes and establishes an audit committee with authority, responsibility, and specific duties as described below.

Composition

The committee shall be comprised of three directors who are independent of management and operating executives. Their terms shall be staggered so that the committee annually includes a new member, and members with one and two years of service. One of the members shall be appointed committee chairman by the chairman of the board of directors.

Authority

The audit committee is granted the authority to perform each of the specific duties enumerated in this committee charter and, upon the direction and approval of the board of directors, to investigate any activity of the company; however, the chairman of the board of directors may, from time to time, appoint a select committee of independent directors to make specific investigation. All employees are directed to cooperate as requested by members of the committee. The committee is empowered to retain persons having special competence as necessary to assist the committee in fulfilling its responsibility. However, the committee will notify the board of directors of such action and, if appropriate, receive board approval before proceeding.

Responsibility

The audit committee is to serve as a focal point for communication between noncommittee directors, the independent accountants, internal audit, and corporate management, as their duties relate to financial accounting, reporting, and controls. The audit committee is to assist the board of directors in fulfilling its fiduciary responsibilities

as to accounting policies and reporting practices of the company and all subsidiaries and the sufficiency of auditing relative thereto. It is to be the board's principal agent in assuring the independence of the corporation's independent accountants, the integrity of management, and the adequacy of disclosures to stockholders. The opportunity for the independent accountants to meet with the entire board as needed is not to be restricted, however.

Meetings

The audit committee is to meet at least three times per year, and as many times as that committee deems necessary.

Attendance

Members of the audit committee are to be present at all meetings. As necessary or desirable, the chairman may request that members of management, the director of internal audit, and representatives of the independent accountants be present at meetings of the committee.

Minutes

Minutes of each meeting are to be prepared and sent to committee members and to directors who are not members of the committee. If the secretary of the corporation has not taken the minutes, they should be sent to him or her for permanent filing.

Specific Duties

The audit committee is to

1. Inform the independent accountants and management that the independent accountants and the committee may communicate with each other at all times; and the committee chairman may call a meeting whenever he deems it necessary.

2. Review with the company's management, independent accountants, and director of internal audit, the company's general policies and procedures to reasonably assure the ade-

quacy of internal accounting and financial reporting controls.

3. Have familiarity, through the individual efforts of its members, with the accounting and reporting principles and practices applied by the company in preparing its financial statements. Further, the committee is to make, or cause to be made, all necessary inquiries of management and the independent accountants concerning established standards of corporate conduct and performance, and deviations therefrom.
4. Review, prior to the annual audit, the scope and general extent of the independent accountants' audit examination, including their engagement letter. The auditors' fees are to be arranged with management and annually summarized for committee review. The committee's review should entail an understanding from the independent accountant of the factors considered by the accountant in determining the audit scope, including:
 - Industry and business risk characteristics of the company;
 - External reporting requirements;
 - Materiality of the various segments of the company's consolidated and nonconsolidated activities;
 - Quality of internal accounting controls;
 - Extent of involvement of internal audit in the audit examination;
 - Other areas to be covered during the audit engagement.
5. Review the extent of nonaudit services provided by the independent accountants in relation to the objectivity needed in the audit.
6. Review with management and the independent accountants, upon completion of their audit, financial results for the year prior to their release to the public. This review is to encompass:
 - The company's annual report to shareholders for Form 10-K, including the financial statements, and financial statement and supplemental disclosures required by generally accepted accounting principles and the Securities and Exchange Commission;
 - Significant transactions not a normal part of the company's operations;
 - Changes, if any, during the year in the company's accounting principles or their application;
 - Significant adjustments proposed by the independent accountants.
7. Evaluate the cooperation received by the independent accountants during their audit examination, including their access to all requested records, data, and information. Also, elicit the comments of management regarding the responsiveness of the independent accountants to the company's needs. Inquire of the independent accountants whether there have been any disagreements with management which if not satisfactorily resolved would have caused them to issue a non-standard report on the company's financial statements.

8. Discuss with the independent accountants the quality of the company's financial and accounting personnel, and any relevant recommendations which the independent accountants may have (including those in their "letter of comments and recommendations"). Topics to be considered during this discussion include improving internal financial controls, the selection of accounting principles, and management reporting systems. Review written responses of management to the "letter of comments and recommendations" from the independent accountants.
9. Discuss with company management the scope and quality of internal accounting and financial reporting controls in effect.
10. Apprise the board of directors, through minutes and special presentations as necessary, of significant developments in the course of performing the above duties.
11. Recommend to the board of directors any appropriate extensions or changes in the duties of the committee.
12. Recommend to the board of directors the retention or nonretention of the independent accountants, and provide a written summary of the basis for the recommendations.

A Food Company

The Audit Committee performs the function of monitoring on behalf of the board of directors the adequacy and effectiveness of the internal and external audit functions, control systems, financial accounting and reporting, and adherence to applicable legal, ethical and regulatory requirements. The committee's specific responsibilities include the following:

A. Independent Public Accountants:

1. Recommend to the board the selection of the independent public accountants for the annual audit, giving consideration to independence, effectiveness and cost.
2. Approve, in advance, the planned scope of the examination of the company's financial statements by the independent accountants.
3. Approve, in advance, non-recurring services to be performed by the independent accountants.
4. Meet privately at least annually with the independent accountants to review the adequacy of the company's internal controls, accounting policies and procedures and the internal audit function.

B. Internal Audit, Accounting, and Reporting:

1. Review with management the adequacy of the company's systems of internal control to provide reasonable assurance that assets are safeguarded, prescribed policies and procedures are followed and transactions are properly recorded and reported.

2. Review and approve major changes in the duties and responsibilities of the corporate controller and the company's accounting policies, principles or practices.
3. Review recommendations of the independent accountants resulting from the audit to be sure that appropriate actions are taken by management.
4. Review the activities, plans, responsibilities and capabilities of the internal audit function.
5. Review with management and/or the independent accountants any matter of disagreement between management and the independent accountants.
6. Review with management the status of tax returns and tax audits.
7. Review officers' reimbursed expenses and perquisites with regard to their proper reporting and accounting.

C. Legal and Ethical Conduct, and Conflicts of Interest:

1. Review the company's policies and practices related to compliance with the law, ethical conduct and conflicts of interest, to be satisfied that such policies are adequate and are adhered to by the company.
2. Review current or pending litigation involving the company which may have a material financial impact on the company or relate to matters entrusted to the committee.

D. Security:

Review the company's policies and practices related to security of assets, information and key personnel to be satisfied that such policies are adequate and are adhered to by the company.

E. Special Investigations:

Direct any special investigations concerning matters relating to the company's financial statements, internal controls, compliance with the law or business ethics.

The committee shall be available at all times to receive suggestions, questions or recommendations from the independent public accountants, the general auditor, the controller or general counsel.

The committee will report to the full board in writing at least annually on the activities and findings of the committee.

A Petroleum Company

RESOLVED, That the objectives of the Audit Committee are:

1. to assist the board of directors in fulfilling its fiduciary responsibilities relating to the company's financial reporting standards and practices,
2. to determine the adequacy of and promote the company's continued emphasis on internal financial controls,
3. to maintain open, continuing and direct communication between the board of directors and both the com-

pany's independent public accountants and its internal auditors, and

4. to instigate any special investigations of conflicts of interest, and compliance with federal, state and local laws and regulations, including the Foreign Corrupt Practices Act, as may be warranted, and be it further

RESOLVED, That the primary operating policies of the Audit Committee are:

1. The Audit Committee shall be composed of three or more outside members of the board of directors. Members of the Audit Committee shall be appointed and removed and the chairman of the committee shall be elected by action of the non-employee members of the board of directors.
2. The Audit Committee shall hold such meetings as deemed necessary but shall endeavor to meet a minimum of three times per calendar year. Minutes of all committee meetings shall be taken and approved at subsequent meetings.
3. Upon the request of the independent public accountants or the company's general auditor, the chairman of the Audit Committee shall convene a meeting of the committee to consider any matters such auditors believe should be brought to the attention of the committee, directors or stockholders.
4. The Audit Committee has the authority to direct and supervise an investigation into any matter, including the authority to retain outside counsel or other professional services, and be it further

RESOLVED, That the functions of the Audit Committee shall be to:

1. Recommend to the board of directors the selection, retention and, when necessary, the termination and replacement of the principal (and/or other) firm (or firms) of independent public accountants (i.e., external auditors) to examine the consolidated financial statements of the company.
2. Review with the principal external auditors their audit plans and scope for the coming year and any non-audit services performed or planned. The committee shall review the compensation paid the external auditors for all audit and other services performed.
3. Review with the external auditors the audit report and their comments arising from the audit.
4. Review with the company's general auditor the internal audit organization and the internal audit goals and plans and discuss the findings and recommendations resulting from internal audits.
5. Review with the company's controller the responses taken to the audit findings and the adequacy of the systems of internal financial control.
6. Review the company's proxy statement and the annual report to stockholders and to the Securities and Exchange Commission.
7. Review with the company's financial management on a periodic basis any changes in accounting principles

significantly affecting the company.

8. Review with the company's financial management any unusual, non-operating and/or non-recurring items and the general quality of earnings reported by the company.

A Metals Company

The Audit Committee shall be responsible for reviewing the adequacy of corporate financial reporting, accounting systems and controls, security of data processing systems and records, and the internal and external auditing functions. The committee shall also maintain a direct and separate line of communication between itself and the internal and external auditors. The committee shall consist of at least four members all of whom shall be nonmanagement directors. One committee member shall be selected as chairman by the Nominating Committee and approved by the board of directors. None of the committee members shall serve on the committee for more than four consecutive years; provided, however, that a committee member may be reappointed to the Audit Committee after a lapse of membership on the committee for a period of at least one year. The terms of the committee members shall be established on a stagger basis so that at least one new member is appointed to the committee at each annual meeting of the board. The committee shall meet at least three times annually and additional meetings shall be held upon the call of the committee chairman. The controller, manager-internal audit and a representative from the external auditor shall attend each committee meeting. The general counsel and secretary or alternate shall attend meetings of the Audit Commitment for the purpose of providing counsel and preparing minutes of the meetings and performing other duties as required. Non-committee members may be excused from attendance at any meeting or portion of any meeting of the Audit Committee by the committee chairman.

In order to accomplish its purpose, the committee shall do the following:

1. a. Recommend to the board of directors each year the particular firm to be employed as external auditor to examine and report upon the financial statements of the company (hereinafter referred to as "external auditor").
- b. Approve the appointment of other external auditors employed for specific audit purposes other than that listed in 1.a.
2. Meet with the external auditor prior to the commencement of the annual audit examination each year and discuss:
 - a. The adequacy of the scope of the audit.
 - b. The adequacy of the company's accounting principles, policies, security and practices, and any contemplated material changes thereto.
 - c. New developments in accounting principles or reporting practices which may materially affect the company.

- d. The audit fees—but not to set same.
3. Review the scope of the internal audit program to be performed each year.
4. Review and approve non-audit activities to be performed by the external auditor prior to the commencement of such activities. Also consider what effect, if any, said activities will have on the external auditor's independence.
5. Review all internal and external audit reports and any written management responses thereto.
6. Review annually (a) the expense reports of the chairman of the board and chief executive officer, (b) a summary report of expenses incurred by other executive officers and (c) the use of the company aircraft by executive officers.
7. Periodically review the following:
 - a. Conflict of interest statements.
 - b. Litigation in which the company is involved or may become involved.
 - c. Questionable uses of corporate assets.
8. Prior to submitting the annual consolidated financial statements to the board of directors for final approval, review and discuss with the external auditor and company financial management:
 - a. The results of the completed annual audit.
 - b. The external auditor's overall evaluation of the annual financial statements.
 - c. Financial management's overall evaluation of the annual financial statements.
9. Discuss with external and internal auditors annually:
 - a. The adequacy of internal accounting controls and procedures.
 - b. Suggestions for improvements in accounting, data processing, financial and operating controls as expressed in the external auditor's annual letter to management.
 - c. The extent to which any previously identified control and procedural weaknesses have not been corrected and the reasons why.
 - d. The adequacy of the company's annual and interim reporting practices and external auditor's views concerning the quality of reports to shareholders.
10. Review with the external auditor at least annually their evaluation of the technical competence and adequacy of the company's financial department staff.
11. Examine and consider such other matters in relation to the internal and external audits of the company's accounts and in relation to corporate accounting and reporting matters as the committee may, in its own discretion, determine to be desirable.
12. Regular committee meetings shall be held as follows:
 - a. In April, prior to the beginning of the annual audit.
 - b. In August, after the completion of the annual audit and the preparation of the annual consolidated financial statements.
 - c. In October, after completion of the external auditor's

management letter and the company's response thereto.

13. Perform such other functions which from time to time may be assigned to it by the board of directors.

An Energy Company

The Audit Committee ("the committee"), under delegation of authority by the board of directors, shall (a) assist the board of directors in the discharge of its fiduciary responsibilities relating to the company's accounting principles, reporting practices and internal controls; (b) maintain a direct line of communication with the company's internal and external auditors, and assess their performance and (c) recommend the appointment of independent auditors for consideration by the shareholders of the company.

Membership

The committee shall be comprised of a minimum of three unaffiliated directors. The board of directors shall, at its annual organizational meeting, appoint the chairman and, when feasible, a minimum of one but not more than two new members to the committee. Membership on the committee should be rotated periodically, the objectives of which shall be twofold:

1. To provide new perspectives for deliberation by the committee; and
2. To aid in the alleviation of the committee's copious work demands.

Duties and Responsibilities

- A. Recommend to the board of directors a firm of independent auditors to be engaged by the company.
- B. Review and approve the fee, scope and timing of the audit and other related services rendered by the independent auditor.
- C. Review with the independent auditors, upon completion of their audit:
 1. contents of their report;
 2. adequacy of the company's financial and auditing personnel;
 3. cooperation received during the audit;
 4. company resources used;
 5. significant transactions outside of normal company business;
 6. changes in accounting principles and practices; and
 7. significant proposed adjustments and recommendations for improving internal accounting controls, principles or management systems.
- D. Review the non-audit services provided by the independent auditor.
- E. Approve the selection and/or discharge of the general auditor and appraise his/her performance annually.
- F. Review and approve the internal audit plan.
- G. Review the highlights of significant internal audit find-

ings and recommendations, and management's response thereto.

- H. Review the appropriateness and soundness of the company's policies and practices with respect to internal auditing, accounting and financial controls.
- I. Review the company's quarterly earnings, including the impact of unusual items and changes in accounting principles and estimates.
- J. Review and approve the financial sections of the annual report to shareholders, the SEC Form 10-K and appropriate proxy material.
- K. Review, appraise and report to the board of directors existing difficulties and problems with regulatory agencies which are likely to have a significant financial impact.
- L. Review compliance under the company's business conduct policies. Periodically review these policies and recommend to the board of directors changes which the committee may deem appropriate.
- M. Review the application of policies and procedures used to handle various matters for which conflicts of interest could arise in connection with the company's master limited partnership.
- N. Periodically review the company's financial and auditing staff, accounting and auditing procedures and the extent to which recommendations made by the internal audit staff or by the independent auditors have been implemented.
- O. Receive and review reports from the general counsel relating to legal compliance.

Lines of Communication

The general auditor and the independent auditor shall have a direct line of communication to the committee and may bypass management if deemed necessary. The general counsel shall report directly to the committee with regard to legal compliance. The committee may contact directly any employee in the company as it deems necessary, and any employee may bring before the committee matters involving questionable, illegal or improper practices or transactions.

The committee shall report to the board of directors on the fulfillment of its duties under the mandate delegated to it by the board of directors.

Meetings

The committee shall meet at least once each quarter and at such other times as may be requested by its chairman.

Required meetings with the independent auditor are as follows:

- | | |
|------------------|-------------------------------------------------------------------------------------------------------------------------------------------|
| <i>March</i> | Review the audit results, the auditor's opinion, the auditor's perception of the adequacy of the financial staff, and other observations. |
| <i>September</i> | Review the actual fees for the prior year and the scope and estimated fees for the coming year. |

November Review significant management letter items.

Meeting Attendance

The following management representatives should attend all meetings except executive sessions and private sessions with the independent auditors:

Executive Vice President (Principal Financial Officer)
Senior Vice President, General Counsel
Corporate Comptroller
General Auditor

Other management representatives shall attend as necessary.

Supporting Material and Agendas

The committee secretary (the general auditor) and the executive vice president shall prepare a tentative agenda and circulate it among the Audit Committee members. The chairman of the committee has the final say regarding the agenda items.

The agenda and all materials to be reviewed at the meetings should be in the hands of the Committee members at least by the weekend preceding the meeting day.

The committee secretary should coordinate all mailings to the committee members, to the extent practicable.

A Savings and Loan Association

1. Statement of Policy

The board of directors has oversight responsibilities to ensure the association maintains an adequate system of internal control and financial reporting, and is in compliance with all applicable laws and regulations. Through this charter, the board delegates certain duties and responsibilities to the Audit Committee (Committee) to assist it in fulfilling these responsibilities.

The primary responsibilities of the committee are to 1) oversee the association's system of internal accounting control and the financial reporting process, 2) review the internal audit function, 3) select the association's independent auditors, and 4) review all audit reports. These and other areas of responsibility are described later in more detail.

To discharge its oversight responsibilities effectively, the committee will maintain open lines of communication with the chief financial officer, chief internal auditor, and with the association's independent auditors.

The board recognizes that an informed and vigilant audit committee represents an effective influence for ensuring adequate internal controls and fair and complete financial reporting. The members of the committee are expected to discharge their duties with the same good faith, diligence, care and skill expected of the other directors of the association.

II. Organization and General

A. The committee shall be composed of not less than three

and no more than five non-management directors.

B. The committee shall have a chairman, appointed by the board of directors. The chairman shall conduct and preside at each meeting of the committee. The committee shall appoint a secretary who shall keep a record of the committee's proceedings.

C. The committee shall meet at least once each quarter to review the financial statements, the activities and reports of the internal auditor and the independent auditor, and other matters requiring consideration by the committee. The committee chairman may call other meetings during the year as necessary.

D. The committee shall have the power to adopt its own operating rules and procedures and to call upon assistance from officers and employees of the Association.

E. The committee shall report its activities to the full board following each meeting of the committee to keep the board informed of all committee activities and findings on a current basis.

III. Duties and Responsibilities

A. Oversight of Internal Accounting Controls

The committee shall be responsible for overseeing the association's internal accounting controls. These controls should be designed to assure that assets are safeguarded, transactions are authorized, and that transactions are properly recorded. Senior management, the chief internal auditor, or the independent auditors may be called on to discuss the accounting control system and changes thereto as may be needed.

B. Review of Internal Audit

1. The committee shall review the annual internal audit plan with the chief internal auditor. The review shall focus on the scope and effectiveness of internal audit activities and the department's capacity to fulfill its objectives. The committee shall inquire as to the extent the planned audit scope can be relied upon to detect fraud or weaknesses in internal controls.

2. The committee shall review all internal audit reports, including management replies, and the status of any corrective actions taken by management.

3. The committee shall meet privately with the chief internal auditor at each meeting, and with the independent auditor at meetings, the independent auditor presents the audit plan or presents audit findings.

4. The committee shall have final authority over the appointment and dismissal of the chief internal auditor.

C. Independent Auditors

1. Management shall recommend to the committee the selection, retention, or change in the association's independent auditor. The committee shall, after due consideration of management's recommendations, make the recommendation to the board concerning the selec-

- tion, retention or change of the independent auditor.
2. The independence of the independent auditor shall be reviewed periodically with management and with the independent auditor. To assist the committee, management shall inform the committee of all plans to engage the independent auditor to perform management advisory services or other non-audit services for the Association.
 3. The committee shall meet with the independent auditor prior to the audit examination to discuss the audit plan, including the scope, staffing and timing of the audit, extent of coordination with internal audit, and discussion of prior audit problems and consideration of other problems that may be expected during the upcoming audit.
 4. The committee shall meet with the independent auditors subsequent to each audit to review any significant auditing or accounting problems encountered during the audit, and the level of support provided by the association's accounting and internal audit staffs. The independent auditor will also review with the committee any audit findings concerning the adequacy of system of internal controls and compliance therewith, including the responses provided by management of any such findings.

D. Oversight of Financial Reporting

1. The annual audited financial statements of the association and each of the quarterly unaudited financial statements shall be reviewed by the committee. The purpose of the review shall be to evaluate the financial reporting process to ensure that the financial statements fairly present the financial position and results of operations of the association in accordance with generally accepted accounting principles, consistently applied. The committee shall inquire as to the following:
 - Significant variations in financial information between reporting periods.
 - Changes in accounting standards or rules promulgated by the Financial Accounting Standards Board or Securities and Exchange Commission that have an impact on the financial statements.
 - Estimates made by management having a material impact on the financial statements.

E. Other

2. The committee shall review annually management's plan for determining compliance with the Corporate Code of Conduct.
3. The committee shall help assure that the association is operating in accordance with applicable laws, regulatory policies and guidelines as they relate to the functions and responsibilities of the audit committee.
4. Where appropriate and indispensable to protect the assets of the association and the interests of the stock-

holders, the committee shall have the authority to engage adequate resources and have standing authority to initiate investigations, including the authority to retain counsel or other outside experts.

5. Periodically review fees paid for external audit services.

A Savings Bank

Purpose: This document is to provide direction and guidance to govern the activities of the Audit Committee formed by resolution of the board of directors.

Scope: It is the intent of the board of directors to furnish hereby a reference source concerning the basis of establishing an Audit Committee and specifying the authority, composition, meeting requirements, primary functions, and procedures for recording and reporting the activities of the committee.

Basis: Federal Home Loan Bank Board Memorandum - R 44, dated May 22, 1978, subject: "Audit Committees of Boards of Directors."

Authority: The intent of the board of directors is to have the Audit Committee serve to monitor selected internal bank affairs for the board. The committee is authorized to seek facts, form opinions, report findings to the board, and, if called for, make recommendations to the board for consideration. The Audit Committee is not empowered to take action, make decisions, or otherwise act for the board of directors in any way affecting the operations of the bank. The Audit Committee reports to the board and ultimately to the stockholders.

Composition: The Audit Committee shall be comprised of members of the board of directors appointed by resolution of the board. The Audit Committee shall have at least three members. All directors shall be eligible to serve on the Audit Committee except those directors who are employed by the association in a management position.

Meetings: There is no intent to limit or control the number, location, or nature of the meetings held by the audit committee. However, the following guidelines are established:

- a. The Audit Committee shall meet at least once each quarter.
- b. Normally, meetings should be held at the offices of the bank.
- c. The Audit Committee may have available at meetings any operating personnel desired by the committee. However, to provide support and information, the chairman of the board, president, vice president of lending, marketing director, and the chief financial officer/controller will be available to the committee upon request.
- d. The Audit Committee, upon request, may have the independent auditors in attendance at any meeting.
- e. The chairman of the board of directors may be present at any meeting.
- f. By request to the chairman of the board prior to meetings, the committee can have available any documents or reports for reference or examination.

Primary Functions: The Audit Committee is to assist the board of directors by providing detailed examination and monitoring of activities relating to the independent auditor, internal controls, security, budgeting and financial reporting. To carry out these functions, the committee activities are to include, but are not limited to, the following.

The committee assumes the board's responsibility for financial and internal control. This is not to imply that the full board is absolved of financial responsibility, but only that the Audit Committee bears the primary responsibility for monitoring these areas and relating findings to the full board.

With respect to the Audit Committee, the Audit Committee will:

- a. Review the results of audits and activities of the internal auditor.
- b. In consultation with senior management, recommend the selection of the bank's independent auditors to the board.
- c. Review the scope of the yearly exam with the independent auditors prior to the commencement of the audit. Areas that should be discussed are:
 1. Time frame for the audit.
 2. Special risk areas that will require special attention.
 3. Independence of the auditors.
 4. Fees for the audit.
 5. Current accounting principles.
- d. Review the complete audit report with the auditors after the audit. Areas that should be discussed are:
 1. Time and/or fee variances.
 2. Management letter recommendations.
 3. Whether or not management cooperated fully by providing all information and explanations that were requested.
 4. Financial statement analysis.
 5. Status of internal control.
- e. Report to the board the result of the committee review, with particular emphasis on any items which are judged to warrant special consideration by the board.
- f. With respect to the annual Federal Home Loan Bank examination, the Audit Committee will:
 1. Review the final report from the FHLB.
 2. Review management's response to the final report.
 3. Discuss with management any plans (if necessary) to rectify problems noted in the report.
 4. Report to the bank.
- g. Review the nature and impact of any proposed changes in accounting policies or principles, with particular emphasis on the effect of such proposals on financial statements of the bank.
- h. Review the proposed annual operating budget with the managing officer and other appropriate operating personnel. Inform the board of the result of the committee's review when the annual budget is presented to the board for action.
- i. Each quarter, review with management the budget variance analysis for the quarter and year-to-date. Report to the board any significant information deemed appropriate for board consideration.
- j. With assistance as needed from the internal auditor, observe and monitor selected internal control measures as desired. Bring to the attention of the managing officer any item judged in need of improvement.
- k. Monitor the adequacy of the security provisions and procedures of the bank.
 1. Upon request by the managing officer, provide detailed interface knowledge to the board on a project, proposal or report deemed appropriate by the managing officer.
- m. Review with senior management the annual stockholders report and each quarterly report prior to publication.
- n. Review with management the bank's insurance coverage on a semi-annual basis.
- o. Review with management the data center's independent third party review annually.
- p. Perform other projects that may be requested by the full board, the chairman of the board, or the president.

Records and Reports: The Audit Committee will be required to maintain separate minutes. The intent of the board of directors is to have the Audit Committee serve to monitor selected internal bank affairs for the board. The committee is authorized to seek facts, form opinions, report findings to the board, and, if called for, make recommendations to the board for consideration. The Audit Committee is not empowered to take action, make decisions, or otherwise act for the board of directors in any way affecting the operation of the bank.

A Bank Holding Company

Preface

The principal responsibilities of the Auditing Committee and the Trust Examining Committee, hereinafter referred to as the Committee, are to satisfy itself on behalf of the board of directors as to the soundness of the asset position and the accuracy and integrity of the financial reporting structure of the committee and its subsidiaries, and to determine that operations are conducted on an ethical basis and in compliance with all applicable laws, rules and regulations.

It should be noted that the committee is not primarily responsible for the quality of credits or investments nor expected to correct any deficiencies in operations or financial reporting. This responsibility rests with the management of the corporation, who must take all necessary action to maintain the integrity of assets, operate the business consistent with sound and proper practices, and take corrective action when necessary.

The existence of the committee and the delegation to it of certain powers and duties by the board of directors does

not relieve any individual member of the board of directors from his responsibility to satisfy himself that the affairs of the corporation are being properly conducted.

The minutes of all meetings of the committee together with all supporting schedules and data received and reviewed by the committee are available for examination by any directors upon request to the secretary of the committee. Subject to this understanding, the manner in which the committee will discharge its responsibilities is set forth in the following paragraphs.

Independent Auditors

The committee will review and approve where appropriate the following reports of the independent auditors:

- (1) Reports on the limited review of unaudited quarterly financial statements;
- (2) A written summary submitted in advance of each annual audit outlining the scope of such audit and the audit plan;
- (3) The results of the annual audit, including all criticisms and suggestions.

The committee will recommend to the board of directors each year the retention or otherwise of the independent auditors, and will review their fees for services.

In those instances where it is necessary to retain independent public accountants other than the principal firm of public accountants employed by the corporation to perform auditing services (ordinarily overseas) the determination of the scope of such audits, the fees to be paid, and the administrative relationship to be maintained with such public accountants shall be the responsibility of the general auditor, who shall keep the committee fully informed as to the findings and recommendations of such public accountants. Selection and retention of such public accountants for the conducting of such audits shall be the joint responsibility of the general auditor and the executive vice president-world banking, as approved by the committee.

Internal Auditing and Credit Examining

The committee will review on a quarterly basis the internal reports of the chief credit examiner and of the general auditor with the understanding that any unusual happenings in areas under their respective jurisdictions will be brought to the immediate attention of the committee. All such internal reports will be transmitted to the committee with an appropriate covering letter of transmittal summarizing the activities reviewed and noting any adverse trends, deficiencies, or evidence of deterioration in either the accounting and control structures of the corporation, or in the policies and practices governing the extension of credit.

The committee will concur in the selection, retention, and compensation of the chief credit examiner and the general auditor, the nature of the work to be performed, and the size and adequacy of their respective staffs.

Outside Examining Agencies

Members of the committee will be furnished immediately upon receipt with a copy of all examinations/audit reports from the Comptroller of the Currency, Federal Reserve Bank, Federal Deposit Insurance Corporation, state banking departments, and any other regulatory authorities with jurisdiction in the area of the committee's responsibilities. See exception below.

The committee will review all such reports promptly and will be furnished with copies of management acknowledgment and responses on a timely basis where such is required. The monitoring of such responses is the responsibility of the general auditor, who shall report at each meeting of the committee as to the current status of any reports requiring response where such response has not been made.

Major reports normally reviewed in this category include the following:

<i>Area Examined</i>	<i>Examining Agency</i>
	Comptroller of the
	Currency
Principal Subsidiary Bank	
International (World	
Banking)	"
Electronic Data Processing	"
Consumer Credit	"
Foreign Offices	"
Trust Division	"
Parent Corporation	Federal Reserve Bank
International Bank	"

Copies of examination/audit reports of agencies other than those detailed above need not be sent to members of the committee if in the judgment of the general auditor they contain no material adverse criticisms or significant recommendations. In such instances the general auditor will make suitable reference to the receipt of such examinations/audit reports in his next quarterly written report to the committee.

Other Reports to be Furnished to the Committee:

Within 90 days of the close of each fiscal year, or within 90 days of June 30 in each year, the committee will be furnished with a detailed report of the following:

- (1) A schedule of all loans and commitments to directors and companies affiliated with directors showing the amount, rate, repayment schedule, and collateral applicable to such loans and commitments as of the end of each fiscal year (6/30).
- (2) A list of all loans/commitments of the bank of \$5 million or more and of the mortgage company of \$2 million or more (6/30).
- (3) A schedule of all loans or securities sold with liability to repurchase all or any part, or with recourse in any way to the bank, the mortgage company, and the credit company (12/31).

- (4) A schedule of all loans to officers of other banks in excess of \$100,000 showing the amount, rate, repayment schedule, and collateral applicable to such loans.
- (5) A schedule of all loans other than those reported in (4) above in excess of \$100,000 secured by the stock of other banks showing the amount, rate, repayment schedule, and collateral applicable to such loans (6/30).
- (6) Copies of the statement of indebtedness given to the national bank examiners by each executive officer of the bank.
- (7) A schedule of all travel and expense accounts of executive officers and directors, and of any other officers where the annual amount exceeded \$10,000, listed as to name, title, and amount.
- (8) A detailed schedule showing the composition of "Other Assets" and "Other Liabilities" (12/31).
- (9) A detailed schedule of letters of credit issued for any amount in excess of \$100,000 for any purpose other than the short term financing of the self-liquidating movement of tangibles (6/30).

All such schedules will be furnished to the committee with a covering letter of transmittal from an appropriate senior office of the bank, parent corporation, or other subsidiary as may be applicable.

Other Areas Reviewed:

The committee will review policies and procedures applicable to the following areas:

- (1) Integrity of electronic data processing systems and facilities
- (2) Foreign exchange operations and controls
- (3) Conduct of overseas operations
- (4) Wire transfer

Compliance with Policies:

The Comptroller of the Currency requires written policies to be established by the Bank and approved by the board of directors covering the following areas:

- (1) International loan portfolio management
- (2) Foreign exchange
- (3) Due from foreign banks
- (4) Loan policies and procedures
- (5) Reserve for possible loan losses
- (6) Investment portfolio management
- (7) Bank dealer activities
- (8) Liquidity, asset and liability management

Any significant deviation from, violation or exception to such established policies coming to the attention of any executive officer, the general auditor, or the chief credit examiner shall be promptly reported to the committee by letter addressed to the secretary.

Pending Litigation

Within 90 days of the close of each fiscal year, the committee will be furnished with a letter from the executive vice

president and general counsel summarizing the status of any material pending or threatened litigation, claims and assessments. This letter shall include as an attachment a similar letter addresses by the chief outside counsel of the bank to the independent public accountants, and will elaborate and supplement such letter to the extent necessary.

Compliance with Law

Within 90 days of the close of each fiscal year the executive vice president and general counsel of the bank, the secretary of the bank, and the secretary of the parent corporation will each furnish a letter addressed to the committee stating that to the best of their knowledge and belief the bank, the corporation, and other major subsidiaries are in compliance with all applicable laws, rules, and regulations.

Standards of Business Conduct

The committee will review annually the written policies of the corporation and its subsidiaries applicable to conflict of interest and to the ethical and legal conduct of business as to their adequacy and proper dissemination.

Authorizations

The committee is authorized and empowered by and on behalf of the board of directors to acknowledge by the signature of its members the receipt and review of all reports from supervisory authorities where such acknowledgement is permitted by law.

Meetings

The committee will meet not less frequently than quarterly and as frequently as necessary to perform its duties.

Implementation of Recommendations and Instructions

Copies of minutes of all meetings will be furnished by the secretary to the chairman of the parent corporation and to the president of the bank. It will be their responsibility to initiate any action necessary to be responsive to recommendations and to comply with instructions which may be reflected in said minutes.

Reports to the Board of Directors

- (1) In order to insure that the board of directors is fully informed on a timely basis concerning the activities of the committee, the chairman of the committee will report to the board at the next regular board meeting following any meeting of the committee, and a copy of the minutes of such meeting will be included in the book of exhibits regularly furnished to the board.
- (2) A copy of the complete report of all examinations made by the Officer of the Comptroller of the Currency and the Federal Reserve Bank will be mailed to each member of the committee at the time it is received by the bank and it will be reviewed by the committee at its next meeting.

- (3) A copy of the covering letter of such examinations, directed to the board of directors, will be mailed to each director at the same time as the full report is mailed to members of the committee and directors will be informed that a copy of the full report is available for their review in the office of the secretary of the committee.
- (4) At the board meeting following receipt of the report, the chairman of the committee will review the letter and any other significant comments in the report which were not included in the covering letter. Management will likewise comment on the anticipated course of action in the event there are any significant criticized items.

A Bank Holding Company

RESOLVED that the Audit Committee of the Board of Directors perform the following functions:

- (1) Receive periodic reports from management, the independent auditors, or the internal auditors, assessing the impact of material and significant regulatory changes and accounting developments;
- (2) Review the corporation's consolidated annual financial statements with the independent auditors and management;
- (3) Review, in consultation with the independent auditors, the results of their audit of the corporation, the report of such audit, any related management letter, and management's response to recommendations made by the independent auditors in connection with the audit, and appraise the effectiveness of such external audit;
- (4) Receive and review reports and management letters of independent accountants on all major subsidiaries;
- (5) Review and approve the independent auditors' fees, and the independence of such auditors, and determine that not restrictions are being placed by management on the scope of their examination;
- (6) Review and approve the appointment or reappointment, as the case may be, of the firm recommended by management to be employed by the corporation and its major subsidiaries as their independent auditors;
- (7) Receive and review verbal and/or written reports from the Audit and/or Examining Committees of all major subsidiaries;
- (8) Review reports of examinations by agencies having regulatory authority with respect to the corporation and/or its major subsidiaries, and evaluate management's responses thereto;
- (9) Review litigation involving the corporation, including major litigation involving its subsidiaries;
- (10) Prepare reports as necessary, but in any event at least annually, summarizing the work done by the committee in performing the functions set forth above.

An Electric Utility Company

Purpose

The primary purpose of the Audit Committee shall be to establish and maintain continuing communications between the board and the company's independent auditors, internal auditors and members of financial management. The committee shall have unrestricted access to, and shall be authorized to communicate directly with, each of these groups. The executive vice president and chief financial officer, the treasurer, the comptroller and the manager, internal auditing shall serve as the primary liaisons between the Audit Committee and the company.

Functions

1. The Audit Committee shall be responsible for reviewing the proposed scope of the annual year-end audit with the independent auditors before they begin their examination to determine that management has imposed no restrictions and that problem areas will get special attention.
2. The Audit Committee shall review the results of the annual year-end audit with the independent auditors to determine whether the auditors are satisfied with the financial statements and related disclosures. At the same time, the committee shall obtain sufficient information about the examination to enable it to respond to inquiries by the full board. The board shall rely upon the Audit Committee to recommend whether the financial statements should be approved for inclusion in the annual report.
3. The Audit Committee shall consider the nature of the auditors' report letter and, in situations where other than an unqualified report is contemplated, obtain a complete explanation. The committee shall ascertain that the auditors were not restricted in performing their examination. The Audit Committee shall receive explanations for significant adjustments proposed but not recorded and adjustments recorded but not previously contemplated. The Audit Committee shall determine whether there have been any disagreements that have not been resolved to the satisfaction of either management or the independent auditors. The committee shall be responsible for obtaining all relevant information about the audit and communicating it in a meaningful manner to the full board.
4. The Audit Committee shall familiarize itself with the company's internal controls and ascertain that the independent auditors' recommendations to management have been adequately considered and properly implemented.
5. The Audit Committee shall review contemplated changes in accounting policies and accounting, reporting and auditing proposals promulgated by regulatory and professional bodies. It shall also ascertain the

nature and adequacy of company policies on political contributions, conflicts of interest and compliance with federal, state or local laws and regulations.

6. The Audit Committee shall be responsible for nominating the independent auditors and for recommending their termination. In considering nominations for independent auditors, the committee shall be sensitive to management's special needs, if any, and prior experience with auditing firms.
7. The Audit Committee shall review the scope of non-audit services performed or to be performed by the independent public accountants, as well as the related fees, and consider the possible effect that the non-audit services could have on the independence of the accountants.
8. The Audit Committee shall receive its authority from and report directly to the full board and shall operate with a minimum of restraints.
9. The Audit Committee's role shall be to review and advise but not to make decisions. The committee shall demonstrate a constructive, supportive and advisory approach.
10. The Audit Committee shall be a standing committee and it shall consist of three outside (i.e., non-employee or independent) directors.
11. The chairman of the Audit Committee shall be responsible for developing an agenda of the meeting sufficiently in advance of the meeting to permit all parties to prepare for the matters under consideration. The agenda shall be developed after consultation with the company's independent auditors, internal auditors and members of financial management. The manager, internal auditing shall provide necessary support to the chairman of the audit committee for compiling, typing and distributing the agenda and other items to the members and other attendees. When possible, reports on agenda topics shall be distributed well before the meetings to allow committee members to prepare themselves better and participate on a more informed basis.
12. Normally, the Audit Committee shall meet jointly with the company's independent auditors, internal auditors and members of financial management. Other members of management shall attend meetings of the Audit Committee only when requested by the chairman of the Audit Committee. The Audit Committee may meet with any of these groups individually where they believe the discussion might be inhibited if any members of the other groups were present or for any other reason deemed appropriate.
13. Minutes of the Audit Committee meetings shall be prepared in draft form by the manager, internal auditing for review and approval of the chairman of the Audit Committee. Approved minutes of the meetings of the Audit Committee shall be distributed to all members of the Audit Committee within fifteen days after the subject meeting.

14. As requested, the company shall provide staff support for the Audit Committee. Requests for such staff support shall be made to the manager, internal auditing.

Activities

The Audit Committee shall hold a minimum of three meetings each year. One meeting shall be held in February at the completion of the annual year-end audit and before the annual report is released. Another regular meeting shall be scheduled in May to discuss internal audit activities and other matters. Additional meetings may be scheduled as required at any time during the year.

A Retailing Company

Function

To assist the board of directors in fulfilling its fiduciary responsibility relating to the accounting, financial, and reporting policies and practices of the corporation and its monitoring of employee benefit plans, and to ensure that the corporation's standards of business conduct and ethics are being observed. These functions will be accomplished by:

- Encouraging management to install and maintain comprehensive systems of internal control that are designed to: aid in the prevention or detection of deviations from the corporation's policies; provide reasonable assurance that assets are safeguarded from unauthorized use or disposition; ensure that the resulting books or records are reliable for the preparation of financial statements or other uses;
- Reviewing new (or changes to existing) financial and accounting policies and practices;
- Monitoring reported results of operations and financial position;
- Ensuring that vigorous, objective audit programs are conducted in the preceding areas by both the independent external auditors and the internal auditors.

Duties

1. Accounting and Reporting

Review and authorize proposals by management for new (or changes to existing) policies and practices. Review annual publicly reported earnings and major underlying issues such as reserves, LIFO adjustments, etc. Review the annual shareholders and 10-K reports. Meet privately with the corporate controller at least annually to solicit comments.

2. Independent External Audit

Review management's annual recommendation for appointment of the independent external auditor and make recommendation to the board. Review and approve proposed audit scope for adequacy of coverage. Review and approve non-audit services performed by the independent external auditors for potential impact on their independence. Review results of the audit from a financial

point of view and solicit auditor concerns. Review the independent auditor's letter report relating to status of internal controls and other matters they deem appropriate. Obtain management's response and corrective action plan. Meet privately with the independent auditors at least annually to solicit comments. Review management's evaluation of the independent auditor's audit performance.

3. Internal Audit

Review and approve the annual corporate-wide internal audit plan for adequacy of coverage and coordination with the independent external auditors. Review results of the internal audit effort on an annual basis or more frequently when warranted by specific audits. Meet privately with the corporate chief auditor at least annually to solicit comments.

4. Employee Benefit Plans

Review and evaluate the annual reports of the Plan Investment Committee and Plan Administrative Commit-

tee. Review and evaluate management's recommended appointments to the Plan Committees and make recommendations to the board. Review and evaluate management's recommended appointments of plan actuary and trustees and make recommendations to the board. Review and evaluate Plan Committees' recommendations to the board of substantive plan changes and plan contributions.

5. Other

Obtain and review an annual report from the corporate general counsel on litigation and other matters. Review and monitor the Conflicts of Interest program conducted by the corporate general counsel. Obtain an annual report on the tax and insurance status of the corporation. Review the results of the annual audit of officer and director expenses and perquisites conducted by the independent external auditors and internal auditors. Report to the full board of directors on all matters deemed of interest to them.