

Annex 1: Terms of reference of the Audit and Risk Assurance Committee (ARAC)

June 2021

1 Role of Audit and Risk Assurance Committee

- 1.1 The Ofgem Board has established an Audit and Risk Assurance Committee to support the Board and the Accounting Officer in discharging their respective responsibilities for matters relating to risk management, internal control and governance.
- 1.2 ARAC will provide assurance to the Ofgem Board and the Accounting Officer on any matter that they or the Board consider may put at risk or affect the achievement of Ofgem's strategic objectives, operational effectiveness or licence to operate as an independent regulator.
- 1.3 ARAC will also provide assurance to the Board and the Accounting Officer on any matter that may affect or have affected the financial integrity, financial reporting or internal controls of the organisation.
- 1.4 ARAC will consider the manner in which the organisation ensures and monitors the adequacy of the nature, extent and effectiveness of risk management, financial and internal control systems, and to recommend any necessary improvements.

2 Membership

- 2.1 The Committee shall have a minimum of two members. The Board shall appoint the Chair and the other members, all of whom shall be Non-executive members of the Ofgem Board. In the absence of the Committee's non-executive Board Member who normally chairs the committee, one of the other non-executive Board Members will chair the meeting.

- 2.2 Where possible, at least one member of the ARAC will be a qualified accountant with recent and relevant experience and able to provide a view on the Annual Report and Accounts.
- 2.3 Save where the Chair of the Committee considers it inappropriate or there is any conflict of interest, the following people responsible for the executive leadership of Ofgem finance, risk and assurance controls, shall normally be invited to attend meetings:
- 2.3.1 Accounting Officer also identified as the Chief Executive Officer;
 - 2.3.2 Director of Corporate Services;
 - 2.3.3 Deputy Director Finance and Procurement;
 - 2.3.4 Head of Assurance;
 - 2.3.5 Head of Corporate Finance;
 - 2.3.6 Internal Audit Representative(s);
 - 2.3.7 National Audit Office (External Audit Representative);
 - 2.3.8 General Counsel;
- 2.4 The Audit and Risk Assurance Committee will be provided with a secretariat function by Ofgem Governance and Secretariat Team (GST).

3 Meetings

- 3.1 ARAC will meet at least four times a year. The Chair of the Audit and Risk Assurance Committee may convene additional meetings, as they deem necessary.
- 3.2 In addition, ARAC will meet each year, specifically to review the draft Annual Report and Accounts.
- 3.3 The quorum for any meeting shall be a minimum of two members.
- 3.4 ARAC may ask any other officials of the organisation or external guests to attend to assist it with its discussions on any particular matter.
- 3.5 ARAC may ask any or all of those who normally attend but who are not members to withdraw to facilitate open and frank discussion of particular matters.
- 3.6 The Board or the Accounting Officer may ask the Audit and Risk Assurance Committee to convene further meetings to discuss particular issues on which they want the Committee's advice.
- 3.7 A minimum of fourteen days' notice for a meeting, shall be given to each member in electronic mail and shall specify the time and place of the meeting.
- 3.8 An agenda of business to be discussed and papers, shall as far as possible be sent to each member no later than five working days before the meeting.
- 3.9 A meeting called on shorter notice will nonetheless be valid.
- 3.10 Failure of a member to receive notice of a meeting does not invalidate that meeting or any business transacted at it.
- 3.11 ARAC meetings shall be held – and members may attend its meetings – in person, or via telephone, video link or online platform.
- 3.12 The Governance and Secretariat team (GST) shall maintain a written record of the proceedings, including actions and decisions made.

Consideration by electronic communications

3.13 With the prior approval of the Chair, urgent matters, where expedient, can be considered by way of electronic communications.

3.14 Matters to be considered in this way shall be circulated to all members by email and comments or opinions of members may be provided by email or other electronic means and shall be provided to the Secretariat and all ARAC members.

3.15 Comments and opinions made by any ARAC member(s) on any matter in accordance with this paragraph shall not be invalidated due to the failure of any other ARAC member(s) to provide any comment or opinion in respect of that same matter. For such matters, the Secretariat will maintain a written record in accordance with paragraph 3.12

4 Access

4.1 The Internal Audit representative and the representative of National Audit Office will have free and confidential access to the Chair of the Audit and Risk Assurance Committee.

5 Reporting

5.1 The Audit and Risk Assurance Committee formally report to the Ofgem Board and, in relation to matters affecting the role of Accounting Officer, the Chief Executive Officer.

5.2 Following each meeting, ARAC shall provide a written or oral report to the next meeting of the Ofgem Board and will share the minutes of the Committee meeting as a minimum.

- 5.3 At the end of each financial year, the Chair of the Committee shall produce an annual report for the Chair of the Authority and the Accounting Officer.
- 5.4 The Audit and Risk Assurance Committee will review its terms of reference and effectiveness annually, and recommend any changes it considers necessary to the Ofgem Board for approval.

6 Responsibilities

- 6.1 The Audit and Risk Assurance Committee will be responsible for the following and shall make whatever recommendations it deems appropriate on any area within its remit where action or improvement is needed.

In relation to the Accounting Officer

- 6.2 Review and advise the Accounting Officer on the Governance Statement and the signing of the Annual Report and Accounts.
- 6.3 Review and advise as to the adequacy of risk management procedures and processes.
- 6.4 Review and advise as to the adequacy of the anti-fraud and “whistle-blowing” policy and procedures.

Audit arrangements

- 6.5 Review proposals and make recommendation to the Ofgem Board in relation to the appointment of the internal audit provider.
- 6.6 Advise the Ofgem Board and make recommendation in relation to a programme of audit reviews covering key financial, leadership, management and control processes, underpinning the integrity and effectiveness of Ofgem, taking into account the key risks facing Ofgem.

- 6.6.1 Once approved by the Ofgem Board, any proposed in-year changes to the programme of recommended reviews are delegated to the Audit Risk and Assurance Committee to approve.
- 6.6.2 Any changes will firstly be considered by the Executive Team [having sought the views of the Internal Audit Service provider on the proposed changes], and then presented to ARAC at one of its future meetings for decision.
- 6.6.3 In the event that there is a need for an urgent change to a programme of audits which cannot wait until the next scheduled meeting of ARAC, then the approval to the proposed change can be sought out-of-committee by email to the Chair and non-executive members of the ARAC (the email to confirm that the proposed change is supported by the Executive Team and Internal Audit Service Provider).
- 6.6.4 The Chair of ARAC would then update ARAC as to actions taken at the next meeting of the Committee.
- 6.7 To monitor the results of the internal audits, as well any other assurance reports, that have been brought to the attention of the Committee by any other Authority Committee or the Executive, including the Executive's response to issues identified.
- 6.8 To monitor relationships with external auditors, particularly to ensure that there are no restrictions on the scope of the statutory audit.
- 6.9 To review the activities, findings, conclusions and recommendations of the external auditors, including those arising from external audit outputs other than those arising from the statutory audit of the accounts.
- 6.10 Advise the Ofgem Board and make recommendations, in relation to the content and sign-off of the management response letter to the NAO.
- 6.11 Approve the purchase of non-audit services from contractors who provide audit services.

6.12 To monitor the effectiveness of the Internal and External Audit Services on an annual basis.

Financial Reporting and Control

6.13 Advising on the accounting policies, the accounts, including the process for review of the accounts prior to submission for audit, levels of error identified, and management's letter of representation to the external auditors.

6.14 On behalf of the Ofgem Board, challenge the Accounting Officer, on any matter concerning the financial integrity of Ofgem.

6.15 Examine the manner in which Ofgem ensures and monitors the adequacy of the financial control systems, and to recommend any necessary improvements.

Internal controls and risk management systems

6.16 Regularly monitor, review and advise the Board and the Accounting Officer on the effectiveness of Ofgem's management of risk. This will include:

6.16.1 Advising the Ofgem Board on [Ofgem's] overall risk appetite, tolerance and strategy, risk policies, risk management framework and the principal and emerging risks.

6.16.2 Seek suitable assurances from Ofgem Executive relating to Ofgem's management of risk (opportunities and threats), internal processes for identifying, assessing, managing and monitoring them and ensuring corrective action is taken when necessary.

6.16.3 Monitor, review and advise the Board and the Accounting Officer on the effectiveness of Ofgem's internal controls and governance.

Compliance, whistleblowing and fraud

6.17 To annually review and advise the Board and the Accounting Officer, as to the effectiveness and adequacy of internal 'cyber-risk', anti-fraud and "whistle-blowing" policies and processes, and the actions taken by the organisation in response to adverse incidents.

7 Conflicts of Interest

- 7.1 It is the responsibility of each Committee member to review papers before each meeting and notify the Governance & Secretariat Team if there are any interests which may conflict with their duties as members of ARAC.
- 7.2 Members should not participate in any activity of the Audit and Risk Assurance Committee in relation to which they believe they have a possible conflict of interest without the consent of the Chair of the Audit and Risk Assurance Committee.
- 7.3 At the start of each Committee meeting, Members of ARAC will be asked by the Chair to confirm if they have any conflicts in relation to agenda items.

8 Information expectations

- 8.1 The following provides a guide to the information that may be shared at each Audit and Risk Assurance Committee meeting dependent upon the agenda.
- 8.2 A report summarising any significant changes to the organisation's strategic risks and a copy of the strategic/corporate Risk Register.
- 8.3 In-depth reviews of key areas of risk management.
- 8.4 A progress report from Internal Auditors summarising:
 - 8.4.1 work performed (compared with work planned);
 - 8.4.2 key emerging issues;
 - 8.4.3 management response to audit recommendations;

8.4.4 any changes to the agreed audit plan and;

8.4.5 any resourcing issues affecting the delivery of the objectives of internal audit.

8.4.6 A progress report from the external auditors covering any current audits of Ofgem and emerging findings.

8.4.7 Management assurance reports.