



INTERNAL AUDIT CHARTER

MISSION AND SCOPE OF WORK

The mission of Internal Audit in MERALCO is to provide independent, objective assurance and consulting services designed to add value and improve the operations of MERALCO, Subsidiaries and Affiliates by offering new insights and to help accomplish its objectives by bringing a systematic and disciplined, and risk-based approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Assurance services involve the objective assessment of evidence to provide independent opinions or conclusions regarding governance, risk management, and control processes, systems, operations or other subject matters. The examples of assurance service are the following:

- Evaluating the reliability and integrity of information and the means used to identify, measure, classify and report such information.
- Evaluating the adequacy of and compliance with policies, plans and procedures.
- Evaluating the effectiveness and efficiency in deployment of resources.
- Evaluating operations or programs to ascertain whether results are consistent with established objectives and goals and whether such are being carried out as planned.
- Evaluating the effectiveness and efficiency of the governance and risk management processes.

Consulting services are advisory in nature and are generally performed at the specific request of an internal engagement client. These are intended to add value and improve the organization's risk management and control processes without the internal auditors assuming management responsibility. These include, but are not limited to the following:

- Performing advisory, training, and monitoring services related to readiness and compliance with the required self-assessments and certifications regarding internal controls over financial reporting.
- Fact finding and verification services requiring an independent and objective perspective from outside of the requesting unit.

The role of Internal Audit is to determine whether the structure of risk management, control and governance processes for MERALCO, Subsidiaries and Affiliates as designed and represented by Management are adequate and functioning in a manner that ensures:

- Risks are appropriately identified, managed and/or reported.
- Significant financial, managerial and operating information and operating information is accurate, reliable and timely.
- Employees' actions are in accordance with policies, standards, procedures and applicable laws and regulations.
- Resources are economically acquired, efficiently used, and adequately protected.
- Programs, plans, and objectives are achieved.
- Quality and continuous improvement are fostered in the control processes.
- Significant legislative or regulatory issues are recognized and addressed appropriately.

Opportunities for improving management control, profitability and image of MERALCO, Subsidiaries and Affiliates may be identified during audits and such will be communicated to the appropriate level of Management.

ACCOUNTABILITY

The Chief Audit Executive (CAE) shall be accountable to the Audit Committee and to the Management in the performance of his/her duties and shall:



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- Provide annually an assessment on the adequacy and effectiveness of MERALCO's, Subsidiaries' and Affiliates' processes for controlling its activities and managing its risks in the areas set forth under the mission and scope of work.
- Report significant issues related to the processes for controlling the activities of MERALCO, Subsidiaries and Affiliates, including potential improvements to those processes, and provide information concerning such issues and resolutions.
- Provide information periodically on the status and results of the annual internal audit plan and the sufficiency of Internal Audit's resources.
- Coordinate with and provide independent assurance on other control and monitoring functions (risk management, compliance, security, legal, ethics, environmental, external audit).

RESPONSIBILITY

The CAE has the responsibility to:

- Effectively manage the internal audit activity for MERALCO, Subsidiaries and Affiliates.
- Develop a flexible annual internal audit plan using an appropriate risk-based methodology, including any risks or control concerns identified by Management, and submit that plan as well as periodic updates thereto to the Audit Committee for review and approval.
- Communicate Internal Audit's plans and resource requirements, including significant interim changes, and the impact of resource limitations.
- Implement the annual internal audit plan, as approved, including and, as appropriate, any special tasks or projects requested by Management and the Audit Committee.
- Consider the scope of work of the internal and external assurance and consulting service providers, as appropriate, for the purpose of providing optimal audit coverage to MERALCO, Subsidiaries and Affiliates at a reasonable overall cost.
- Evaluate and assess significant merging/consolidating functions and new or changing services, processes, operations and control processes coincident with their development, implementation, and/or expansion.
- Maintain a professional audit staff with sufficient knowledge, skills, experience and professional certifications, and other competencies to meet the requirements of this Charter.
- Issue periodic reports to the Audit Committee and Management summarizing results of audit activities, including internal audit personnel headcount, movement and professional development.
- Conduct the appropriate follow-up on engagement findings and recommendations which shall remain in an open issues file until cleared.
- Ensure there is appropriate mechanism in place for the anonymous submission of employee concerns or complaints on questionable accounting or auditing matters and notify the Audit Committee of the status and disposition of reported complaints.
- Assist in the investigation of significant suspected fraudulent activities in MERALCO, Subsidiaries and Affiliates and notify Management and the Audit Committee of the results.
- Provide a list of significant measurement goals and results to the Audit Committee.
- Establish and sustain a quality assurance and improvement program for Internal Audit, including the establishment and updating of policies and procedures, to guide the internal audit organization, by which the CAE assures the operation of internal auditing activities, and communicate the results of ongoing internal assessments and external assessments conducted at least every five years.
- Report periodically on Internal Audit's purpose, authority, responsibility and performance relative to its plan and on its conformance with the Code of Ethics and the Standards, including fraud



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risks, governance issues and other matters that require the attention of Senior Management and/or the Board.

- Keep the Audit Committee informed of emerging trends and successful practices in internal auditing.

AUTHORITY

The CAE and Internal Audit are authorized, in MERALCO, Subsidiaries and Affiliates, to:

- Have unrestricted access to all functions, records, property and personnel pertinent to carrying out any engagement, subject to accountability for confidentiality and safeguarding of records and information.
- Have full and free access to and communicate and interact directly with the Audit Committee.
- Allocate resources, set frequencies, select subjects, determine scopes of work and apply the techniques required to accomplish audit objectives and issue reports.
- Obtain the necessary assistance of personnel in units within MERALCO, Subsidiaries and Affiliates where they perform audits as well as other specialized services from within or outside MERALCO, Subsidiaries and Affiliates.

The CAE and staff of Internal Audit are not authorized to:

- Assess specific operations of a unit or department in which an Internal Audit employee was previously part or responsible for in the last twelve months.
- Perform any operational duties for MERALCO, Subsidiaries and Affiliates.
- Initiate or approve accounting transactions except those pertaining to the operation of Internal Audit.
- Direct the activities of any MERALCO, Subsidiaries and Affiliates' employees not employed by Internal Audit, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the internal auditors.

INDEPENDENCE AND OBJECTIVITY

To provide for the independence of Internal Audit, its personnel report to the CAE, who reports functionally to the Audit Committee and administratively to the President and Chief Executive Officer in a manner outlined in the above section on Accountability. The CAE shall confirm to the Audit Committee, at least annually, the organizational independence of the internal audit activity.

The CAE and staff of Internal Audit shall:

- remain free from interference by any element in the organization, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of a necessary independent and objective mental attitude.
- have no direct operational responsibility or authority over any of the activities audited and shall not engage in any other activity that may impair professional judgement.
- exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined.

PROFESSIONALISM AND STANDARDS OF PRACTICE

Internal Audit and its activities shall adhere to The Institute of Internal Auditors' mandatory guidance including the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics for Internal Auditors, the International Standards for the Professional Practice of Internal Auditing, and



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the Definition of Internal Auditing¹.

Approved this 24th day of October 2019.

A handwritten signature in black ink, appearing to read 'Melanie T. Oteyza'.

Melanie T. Oteyza
First Vice President & Chief Audit Executive

A handwritten signature in blue ink, appearing to read 'Ray C. Espinosa'.

Atty. Ray C. Espinosa
President & CEO

A handwritten signature in black ink, appearing to read 'Artemio V. Panganiban'.

Ret. Chief Justice Artemio V. Panganiban
Chairman, Audit Committee

¹ Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.