

Midatech Pharma PLC (the "Company")

AUDIT COMMITTEE - TERMS OF REFERENCE

1. INTRODUCTION

At a meeting of the board of directors of the Company (the "**Board**") held on 3 December 2014 the Board resolved, in accordance with the articles of association of the Company, to establish a committee known as the Audit Committee (the "**Committee**") and approved the following terms of reference for the Committee.

2. CONSTITUTION AND AUTHORITY

2.1 The Committee is authorised to investigate and undertake any activity within these terms of reference. It is authorised to seek any information it properly requires in order to perform its duties from the company secretary, any director, employee or professional adviser (subject to paragraph 2.2 below) of the Company or any subsidiary of the Company (where the term "**subsidiary**" shall be as defined in section 1159 of the Companies Act 2006, the Company and its subsidiaries from time to time being the "**Group**"). It is authorised to call any employee to be questioned at a meeting of the Committee as and when required. All directors, employees or professional advisers (subject to paragraph 2.2 below) of the Company are directed to co-operate with any such request made by the Committee.

2.2 If the Committee considers it necessary so to examine any activity within its terms of reference, it is authorised to obtain appropriate external professional advice including, without limitation, legal and accounting advice to assist it in the performance of its duties, to secure the services of outsiders with relevant experience and expertise and to invite such persons to attend meetings of the Committee. The Committee shall have full authority to commission any reports or surveys which it deems necessary to help it fulfil its obligations. The cost of obtaining such advice or services shall be borne by the Company within such limits as may be authorised by the Board from time to time.

2.3 Each member of the Committee shall disclose to the Committee:

- (a) any personal, financial or other interest in any matter to be decided or discussed by the Committee; and/or
- (b) any potential conflict of interest arising from a cross-directorship or otherwise; and

any such member shall abstain from voting on resolutions of the Committee in relation to which such interest exists and from participating in the discussions concerning such resolutions and (if so required by the Board) shall resign from the Committee or absent himself from all or part of the meeting of the Committee in question.

3. DUTIES OF THE COMMITTEE

3.1 General

The Committee shall carry out the duties set out in this paragraph 3 for the Company, major subsidiary undertakings and the Group as a whole, as appropriate.

3.2 Financial Reporting

The Committee shall:

- (a) monitor the integrity of the financial statements of the Company, including its annual and half-yearly reports, interim management statements, preliminary results' announcements and any other formal announcements relating to its financial performance, reviewing significant financial reporting issues and judgements which they contain;
- (b) review summary financial statements, significant financial returns to regulators and any financial information contained in certain other documents, such as announcements of a price sensitive nature;
- (c) keep under review the consistency of accounting policies both on a year to year basis and across the Company and/or Group;
- (d) review and challenge where necessary the Company's half-yearly and annual financial statements before submission to the Board, focusing particularly on:
 - (i) the consistency of, and any changes to, accounting policies and practices both on a year on year basis and across the Company and the Group;
 - (ii) the methods used to account for significant or unusual transactions where different approaches are possible;
 - (iii) whether the Company has followed appropriate accounting standards and made appropriate estimates and judgements, taking into account the views of the external auditor;
 - (iv) the clarity of disclosure in the Company's financial reports and the context in which statements are made;
 - (v) significant adjustments resulting from the audit;
 - (vi) the going concern assumption;

- (vii) compliance with applicable requirements of the AIM Rules for Companies and any other legal and regulatory requirements;
 - (viii) compliance with the QCA Corporate Governance Code for Small and Mid-Size Quoted Companies 2013;
 - (ix) reviewing the Company's statement on internal control systems prior to endorsement by the Board and to review the policies and process for identifying and assessing business risks and the management of those risks by the Company; and
 - (x) all material information presented with the financial statements, such as the business review/operating and financial review and the corporate governance statement (insofar as it relates to the audit and risk management);
- (e) discuss problems, reservations and recommendations arising from the interim and final audits, and any matters the external auditors may wish to discuss including any matters arising from their work (in the absence of the executive directors and other management, where necessary);
 - (f) make recommendations to the Board of the items that should be published in the Company's annual report relating to the membership of the Committee, number of meetings of the Committee and attendance at those meetings over the course of the year; and
 - (g) review the annual financial statements of the pension funds (if applicable) where not reviewed by the Board as a whole.

3.3 Internal Controls and Risk Management Systems

The Committee shall:

- (a) keep under review and challenge where necessary the adequacy and effectiveness of the Company's internal financial reporting and internal control policies and procedures and risk management systems for the identification, assessment and reporting of risks including the reporting of significant or unusual transactions; and
- (b) review and approve the statements to be included in the annual report of the Company concerning internal controls and risk management and the accounting standards used.

3.4 Compliance, Whistleblowing and Fraud

The Committee shall:

- (a) review the adequacy and security of the Company's arrangements for its employees and contractors to raise concerns, in confidence, about possible wrongdoing in financial reporting or other matters. The Committee shall ensure that these arrangements allow proportionate and independent investigation of such matters and appropriate follow up action;
- (b) review the Company's procedures for detecting fraud; and
- (c) review the Company's systems and controls for the prevention of bribery and receive reports on non-compliance.

3.5 **Internal Audit**

The Committee shall:

- (a) where there is no internal audit function, consider at least once a year, whether there is a need for one. In the event that there is no need for an internal audit function, the reasons for this decision shall be fully explained in the Company's annual report;
- (b) monitor and review the effectiveness of the Company's internal audit function in the context of the Company's overall risk management system;
- (c) approve the appointment and removal of the head of the internal audit function;
- (d) consider and approve the remit of the internal audit function and ensure it has adequate resources and appropriate access to information to enable it to perform its function effectively and in accordance with the relevant professional standards. The Committee shall also ensure the function has adequate standing and is free from management or other restrictions;
- (e) review and assess the annual internal audit plan;
- (f) review promptly all reports addressed to the Committee from the internal auditors;
- (g) review and monitor management's responsiveness to the findings and recommendations of the internal auditor; and
- (h) meet the head of internal audit at least once a year, without management being present, to discuss their remit and any issues arising from the internal audits carried out. In addition, the head of internal audit shall be given the right of direct access to the chairman of the Board and to the Committee.

3.6 **External Audit**

The Committee shall:

- (a) consider and make recommendations to the Board, to be put to shareholders for approval at the annual general meeting of the Company, in relation to the appointment, re-appointment and removal of the Company's external auditor and shall ensure that key partners within the appointed firm are rotated from time to time. The Committee shall oversee the selection process for a new auditor and, if an auditor resigns, the Committee shall investigate the issues leading to this and decide whether any action is required;
- (b) keep under review and oversee the relationship with the external auditor including (but not limited to):
 - (i) considering and making recommendations on their remuneration (whether for audit or non-audit services) and confirming that the level of fees is appropriate to enable an adequate audit to be conducted;
 - (ii) approving their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;
 - (iii) assessing annually their independence and objectivity taking into account relevant professional and regulatory requirements and the relationship with the auditor as a whole, including the provision of any non-audit services;
 - (iv) satisfying itself that there are no relationships (such as family, employment, investment, financial or business) between the auditor and the Company (other than in the ordinary course of business);
 - (v) agreeing with the Board a policy on the employment of former employees of the Company's auditor and then monitoring the implementation of this policy;
 - (vi) having discussions with the external auditors concerning such issues as compliance with accounting standards and any proposals which the external auditors have made vis-à-vis the Company's internal auditing standards;
 - (vii) ensuring that the external auditors report in a timely manner to the Committee on:
 - (A) all accounting policies and practices used or to be used;
 - (B) all alternative disclosures and treatments of financial information within generally accepted accounting principles that have been discussed with management, the ramifications of the use of such alternative disclosures and treatments and the treatment preferred by the external auditor;

- (C) all other material written communications between the external auditors and management, such as any management letter or schedule of unadjusted differences;
- (viii) ensuring that procedures are in place for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters;
- (ix) monitoring the auditor's compliance with relevant ethical and professional guidance on the rotation of audit partners, the level of fees paid by the Company compared to the overall fee income of the firm, office and partner and other related requirements;
- (x) assessing annually their qualifications, expertise and resources and the effectiveness of the audit process which shall include a report from the external auditor on their own internal quality procedures;
- (xi) seeking to ensure co-ordination with the activities of the internal audit function; and
- (xii) considering the risk of withdrawal of the Company's present auditor from the market;
- (c) meet regularly with the external auditor, including once at the planning stage before the audit and once after the audit at the reporting stage to discuss the nature and scope of the audit and to ensure co-ordination where more than one audit firm is involved. The Committee shall meet the external auditor at least once a year, without management being present, to discuss the auditor's remit and any issues arising from the audit;
- (d) review and approve the annual audit plan and ensure that it is consistent with the scope of the audit engagement;
- (e) review the findings of the audit with the external auditor. This shall include, but not be limited to, the following:
 - (i) a discussion of any major issues which arose during the audit;
 - (ii) any accounting and audit judgements;
 - (iii) levels of errors identified during the audit; and
 - (iv) the effectiveness of the audit.

The Committee shall also:

- (a) review any representation letter(s) requested by the external auditor before they are signed by management;
- (b) review the management letter and management's response to the auditor's findings and recommendations; and
- (c) develop and implement a policy on the supply of non-audit services by the external auditor, taking into account any relevant ethical guidance on the matter.

3.7 The Committee shall consider such other matters as may be requested by the Board.

4. **MEMBERSHIP OF THE COMMITTEE**

4.1 The Committee shall comprise at least two members. Members of the Committee shall be appointed by the Board. Both of the members of the Committee (or a majority if the Committee comprises of more than two members) shall be independent non-executive directors of the Company, at least one of whom shall have recent and relevant financial experience. If there are insufficient non-executive directors discounting the chairman of the Board, the chairman of the Board may be a member of the Committee provided that, other than by virtue of his/her chairmanship, one fulfils the test of independence.

4.2 Appointments to the Committee shall be for a period of up to three years which may be extended for two further three year periods by the Board, provided the director in question continues to meet the criteria for membership of the Committee. A member of the Committee may be removed by the Board at any time.

4.3 Only members of the Committee have the right to attend meetings of the Committee. However, other individuals (such as the chairman of the Board, the chief executive, the finance director, any other member of the Board, representatives from the risk, compliance, finance and internal audit functions and external advisers) may be invited by the Committee to attend all or part of any meeting as and when the Committee considers appropriate and necessary but such persons shall have no right of attendance.

4.4 A representative of the external auditors should normally attend all meetings of the Committee. At least once in each year the members of the Committee shall meet the external auditors without the presence of any executive director or other employee of the Company and the Committee shall decide if the executive directors (or any of them) should be present or not at any other meeting attended by the external auditors.

4.5 Care should be taken to minimise the risk of any conflict of interest that might be seen to give rise to an unacceptable influence. Where possible, the Chairman of the Committee and members of the Committee should be rotated on a regular basis.

4.6 Membership of the Committee shall be noted in the annual directors' report of the Company.

5. **CHAIRMAN OF THE COMMITTEE**

5.1 In the absence of the chairman of the Committee and/or an appointed deputy from any meeting of the Committee, the members of the Committee present shall elect one of their number (being a member who would qualify under these terms of reference to be appointed chairman of the Committee by the Board) to chair the meeting.

6. **SECRETARY**

The company secretary or such person as may be nominated by the company secretary or the Committee shall act as the secretary of the Committee.

7. **QUORUM**

7.1 The quorum necessary for the transaction of business at meetings of the Committee shall be two members.

7.2 A duly convened meeting of the Committee at which a quorum is present shall be competent to exercise all or any of the authorities, powers and discretions vested in or exercisable by the Committee.

7.3 Meetings of the Committee may be held by telephone.

8. **FREQUENCY OF MEETINGS**

Meetings of the Committee shall be held at least twice in each financial reporting period at appropriate times in the reporting and audit cycle, at such other times as the chairman of the Committee may require and otherwise as required.

9. **NOTICE OF MEETINGS**

9.1 Meetings of the Committee shall be called by the secretary of the Committee at the request of the chairman of the Committee, any member of the Committee or at the request of the external or internal auditor if they consider it necessary.

9.2 Unless otherwise agreed, notice of each meeting of the Committee confirming the venue, time and date of the meeting, together with an agenda of items to be discussed, shall be forwarded by the secretary of the Committee to each member of the Committee, any other proposed attendee and all other non-executive directors, no later than five working days before the date of the meeting. Supporting papers shall be sent to members of the Committee and, if appropriate, to any other proposed attendee at the same time.

10. **MINUTES OF MEETINGS**

- 10.1 The secretary of the Committee shall minute the proceedings and resolutions of all meetings of the Committee, including the names of those present and in attendance and the existence of any conflicts of interest.
- 10.2 Draft minutes of meetings of the Committee shall be circulated by the secretary of the Committee promptly following the date of the meeting of the Committee to all members of the Committee, the chairman of the Board and the external auditors. When finalised and approved, the minutes shall be circulated to all other members of the Board unless a conflict of interest exists or it would be inappropriate to do so.
- 10.3 The secretary of the Committee shall ascertain, at the beginning of each meeting, the existence of any conflicts of interest and minute them accordingly.
- 10.4 The recommendations of the Committee minutes must be approved by the Board before they can be implemented.

11. **VOTING**

Subject to paragraph 2.3 above, each member of the Committee shall have one vote. In the event of an equality of votes, the chairman of the Committee shall have a second or casting vote (again subject to paragraph 2.3 above).

12. **ANNUAL GENERAL MEETING**

The chairman of the Committee (or another member of the Committee nominated by the chairman of the Committee) shall attend each annual general meeting of the Company to answer any questions from shareholders concerning the Committee's activities.

13. **REPORTING RESPONSIBILITIES**

- 13.1 The Committee shall meet formally, or ensure that the chairman of the Committee meets formally, with the members of the Board at least three times a year to discuss such matters as the Company's annual report and the relationship with the external auditors.
- 13.2 The chairman of the Committee shall report formally to the Board on the proceedings of the Committee after each meeting on all matters within its duties and responsibilities.
- 13.3 The Committee shall make whatever recommendations to the Board it deems appropriate on any area within its remit where action or improvement is needed.
- 13.4 The Committee shall produce a report on its activities to be included in the Company's annual report and accounts and ensure that it is put to shareholders for approval at the annual general meeting of the Company.

14. **OTHER MATTERS**

- 14.1 The Committee shall be given access to sufficient resources in order to carry out its duties, including access to the company secretary for assistance as required.
- 14.2 The Committee shall be provided with appropriate and timely training, both in the form of an induction programme for new members and on an ongoing basis for all members.
- 14.3 In carrying out its duties, the Committee shall give due consideration to all relevant laws, regulations and guidance including the UK Corporate Governance Code, QCA Corporate Governance Code for Small and Mid-Size Quoted Companies 2013, the NAPF Corporate Governance Policy and Voting Guidelines for AIM Companies and the AIM Rules for Companies.
- 14.4 The Committee shall:
- (a) have unrestricted access to the Company's auditors;
 - (b) be responsible for co-ordination of the internal and external auditors;
 - (c) give consideration to dividend policy and payment;
 - (d) oversee any investigation of activities which are within its terms of reference and act for internal purposes as a court of last resort; and
 - (e) have the right to publish in the Company's annual report and accounts details of any issues that cannot be resolved between the Committee and the Board.
- 14.5 The Committee shall, at least once a year, 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.
- 14.6 The Committee shall make available its terms of reference for inspection at the registered office of the Company.
- 14.7 Any of the terms set out in this document may be varied by a majority resolution of the Committee.