

# **Kentucky Bancshares, Inc.**

## **Audit Committee Charter**

### **Statement of Policy**

The Audit Committee is appointed by the Board of Directors to assist the Board in fulfilling its oversight responsibility to the shareholders, investment community, governmental bodies and the public relating to the financial statements and the financial reporting process of the Company, the systems of internal accounting and financial controls, the internal audit function, and the annual independent audit of the Company's financial statements. In so doing, it is the responsibility of the Audit Committee to maintain free and open means of communication between the Committee, the independent auditors, internal auditor, and the management of the Company. In discharging its oversight role, the Committee is empowered to investigate any matter brought to its attention with full access to all books, records, facilities, and personnel of the Company and the power to retain outside counsel or other experts for this purpose. The Company shall provide appropriate funding, as determined by the Audit Committee, for the payment of compensation to the independent auditor for the purpose of rendering or issuing an audit report and to any advisors employed by the Audit Committee.

### **Organization**

The Audit Committee shall consist of no fewer than three members, each appointed by the Board. The members of the Audit Committee shall meet the independence requirements of the Nasdaq Stock Market ("NASDAQ"), Section 10A(m)(3) of the Securities Exchange Act of 1934 (the "Exchange Act"), and the rules and regulations of the Securities and Exchange Commission ("SEC"). Each member shall be financially literate, as defined by NASDAQ, and at least one member shall be a financial expert, as defined by the SEC. One member will be elected by the Board to chair the Committee.

### **Authority and Responsibilities**

The principal responsibilities of the Audit Committee are to oversee the Company's financial reporting process and report the results of its activities to the Board. Management is responsible for preparing the Company's financial statements. The independent auditors are responsible for auditing those financial statements and report directly to the Audit Committee. The Risk Management department is responsible for auditing the internal controls of the Company and reports to the Audit Committee. In carrying out its responsibilities, the Audit Committee should maintain flexible policies and procedures in order to best react to changing conditions. The Committee should take appropriate actions to set the overall corporate tone for quality financial reporting, sound business risk practices, and ethical behavior.

The Audit Committee shall have direct responsibility and authority to:

- Appoint or replace, determine the funding and compensation for, and oversee the work of the Company's independent auditors (including resolving disagreements between management and the auditor regarding financial reporting);
- Appoint or replace and oversee the work of the Company's internal auditors;

- Establish pre-approval policies and procedures for, and pre-approve all audit services and permitted non-audit services performed for the Company by its independent auditors in accordance with section 10A(i) of the Exchange Act and the SEC's auditor independence rules;
- Engage and determine funding for independent counsel and other advisors as the Committee determines is necessary to carry out its duties;
- Establish procedures for the anonymous submission of complaints or concerns by the Company's employees regarding accounting, internal accounting controls or auditing matters, and the receipt, retention and treatment by the Company of those complaints and concerns; and
- Consider transactions involving possible conflicts of interest of the Company's directors and senior officers.
- Ensure there are no unjustified restrictions or limitations with the internal audit activities and the review and concurrence in the appointment, replacement, compensation, and dismissal of the Chief Audit Executive.
- Consider the effectiveness of the internal control system.
- Ensure compliance with laws and regulations with reference to the regulatory bodies.
- Ensure Audit Committee minutes include critical decisions.

In carrying out these responsibilities, the Audit Committee will:

- meet four times per year or more frequently as circumstances require;
- evaluate the qualifications, performance and independence of the independent auditors, including obtaining from the independent auditors and reviewing: (a) a formal written statement delineating all relationships between the auditor and Company, as required by the Independence Standards Board and (b) at least annually a report regarding (i) the independent auditor's internal quality-control procedures, (ii) any material issues raised by the most recent internal quality-control review, or peer review, of the firm, or by any inquiry or investigation by governmental or professional authorities within the preceding five years respecting one or more independent audits carried out by the firm, (iii) any steps taken to deal with any such issues, and (iv) all relationships between the independent auditor and the Company. The Committee should actively engage in a dialogue with the auditors and take appropriate action to oversee the independence and performance of the outside auditors;
- evaluate the qualifications, performance and independence of the internal auditors, including any third party auditors;
- ensure the rotation of the lead (or coordinating) audit partner having primary responsibility for the audit and the audit partner responsible;

- discuss with the independent auditor material issues on which the national office of the independent auditor was consulted by the Company's audit team;
- meet with the independent auditors and financial management of the Company to review the scope and plan of the proposed audit for the current year. At the conclusion of the audit, review significant findings and any comments or recommendations of the independent auditors, including the status of previous audit recommendations, together with management's responses;
- review with the independent auditors, the internal auditor and financial management the adequacy and effectiveness of the accounting and financial controls of the corporation, and any special steps adopted in light of material control deficiencies; and elicit any recommendations for the improvement of such internal control procedures or particular areas where new or more detailed controls or procedures are desirable;
- review the internal audit function of the Company confirming and assuring the objectivity and authority of its reporting obligations, the proposed audit plans for the coming year and the coordination of such plans with the independent auditors;
- receive a summary of findings from completed internal audits, including the findings from any third party audits and a progress report on the proposed internal audit plan with explanations for any deviations from the original plan or any difficulties encountered in the course of audit work;
- review and discuss each quarterly earnings release with management (which, if appropriate, may be performed during the full Board meetings and is not required to be done prior to the filing of the earnings release)
- review and discuss with management and the independent auditors the Company's annual audited financial statements, including the disclosures made in Management's Discussion and Analysis of Financial Condition and Results of Operations, and recommend to the Board whether the audited financial statements should be included in the Company's Form 10-K;
- review and discuss with management and the independent auditors the Company's quarterly financial statements before the filing of its Form 10-Q, including results of the independent auditors' review of quarterly financial statements;
- review and discuss with management and the independent auditors significant financial reporting issues and judgments made in connection with the preparation of the Company's financial statements, including any significant changes in the Company's selection or application of accounting principles;
- review and discuss quarterly reports from the independent auditors on: (i) all critical accounting policies and practices to be used; (ii) all alternative treatments of financial information within generally accepted accounting principles that have been discussed with management, ramifications of the use of such alternative disclosures and treatments, and the

treatment preferred by the independent auditors; and (iii) other written communications between the independent auditors and management, such as any management letter or schedule of unadjusted differences;

- review disclosures made to the Audit Committee by the Company's Chief Executive Officer and Chief Financial Officer during their certification process for the annual 10-K and quarterly 10-Q reports about any significant deficiencies in the design or operation of internal controls or material weaknesses therein and any fraud involving management or other employees who have a significant role in the Company's internal controls;
- meet periodically with the independent auditors, internal auditor and management in separate executive sessions to discuss any matters that the Committee or these groups believe should be discussed privately with the Audit Committee;
- inquire of management, the independent auditors and internal auditor about significant risks or exposures and assess the steps management has taken to minimize such risks for the Company;
- meet periodically with in-house compliance personnel and, as appropriate, with outside legal counsel, about significant risks and exposures, assess the steps management has taken to minimize such risks to the Company, and consider the adequacy of disclosure in the Company's financial statements;
- instruct management and the independent auditors that they must maintain an open and transparent relationship with the Committee, and that the ultimate accountability of the independent auditors is to the Board and the Committee, as representatives of the Company's shareholders;
- submit the minutes of all meetings of the Audit Committee to, and discuss significant results of the foregoing activities with, the Board of Directors; and
- review and reassess the adequacy of this charter annually or as otherwise appropriate.