

Chartered Institute of Internal Auditors
13 Abbeville Mews
88 Clapham Park Road
London, SW4 7BX
Via email: iiapolicy@iia.org.uk

11 October 2019

Dear IIA,

Chartered Institute of Internal Auditors draft Internal Audit Code of Practice

We welcome the opportunity to comment on the Chartered Institute of Internal Auditors draft Internal Audit (IA) Code of Practice ("the Code").

We place great value on the role of IA and the analysis and feedback it provides to the finance function, as well as the assurance it gives to shareholders, the Audit Committee (AC) and wider stakeholders. It is a critical element in ensuring good governance, an area for which UK financial markets are recognised as 'best in class'. In our opinion, IA functions should already be adhering to many of the principles proposed in the Code and as such we are supportive of its implementation. In similarity to the Wates Principles of Corporate Governance, it would be beneficial for there to be one consistent and comparable Code across both listed and private companies.

It's most appropriate for AC's, non-executive directors and shareholders to comment on what they expect from internal auditors and therefore the Code. As CFO's we must remain independent, and as such have only responded to a number of questions raised in the consultation, see appendix one.

We agree the Code should be principles based and have flexibility to ensure that companies are able to apply it as best needed for their risks, structure and resources. We also support the proposals that IA scope should be unrestricted, they should have sufficient and timely access to key management information and should report directly to the board and AC.

We question whether IA should attend and observe the executive committee as it may risk impairing their independence and hence challenge of the business. We believe the right to attend should be determined by the AC. The Code also proposes that IA should include within its scope the information presented to the board and executive management. As drafted it is unclear what the breadth of this review would be, the Code could be more specific, using risk criteria to determine this scope. Moreover a conflict could arise if IA review content whilst also attending the executive meetings.

Across our membership there are variations as to who the secondary executive reporting line is and we believe the Code should be more flexible in this area. Secondary reporting lines will be highly dependent on the organisational structure and risks faced by the company. The Code needs to accommodate for such differences and therefore it should be at the discretion of the AC to appoint the most appropriate secondary executive reporting line.

We have concerns over the proposal of IA auditing in real-time the processes of key events such as acquisitions. Given the timeliness and sensitivity of such events we question how this could be done efficiently and effectively. Assurance is often already obtained by other providers, so there is also risk of unnecessary duplication. We therefore suggest this part of the Code is reconsidered.

Please contact me at brian.gilvary@the100group.co.uk should you wish to discuss our comments.

Yours sincerely,

A handwritten signature in black ink that reads "Brian Gilvary".

Brian Gilvary, 100 Group Chairman

The 100 Group of Finance Directors represents the views of the finance directors of FTSE 100 and several large UK private companies. Our member companies represent almost 90% of the market capitalisation of the UK FTSE 100 Index. Our aim is to contribute positively to the development of UK and international policy and practice on matters that affect our businesses, including taxation, pensions, financial reporting, corporate governance and capital market regulation. Whilst this letter expresses the views of The 100 Group of Finance Directors as a whole, those views are not necessarily those of our individual members or their respective employers.

Appendix 1

1) Which companies, organisations and sectors should the new Internal Audit Code of Practice cover and what should its scope be?

Internal Audit has the potential to contribute to effective risk management and governance in both private and premium listed companies, as well as of course third sector organisations including major charities. We will therefore need to consider carefully which types of organisations the new Internal Audit Code of Practice should apply to.

We will need to consider whether the new Code should be primarily focused on publicly listed companies, or should private companies with an internal audit function also be in scope – particularly large private companies? Going even further than that, should the new Code be extended to third sector organisations? In due course, a Code could also be developed for the public sector.

Whilst the proposal for the scope of the IA Code of practice to apply to both private companies and charities would not affect the 100 Group, we support the notion that good quality governance should be present in all companies. There are a number of advantages to having a Code which is applicable across a range of companies as it enables comparability and consistency. We therefore would support this Code mirroring that of the Wates principles and being applicable to a range of companies.

2) How far should there be independence between the second and third lines of defence?

Does the draft Code adequately reflect the range of practices that organisations have adopted with regard to the existence or not of separate risk and compliance functions? And what does the Code need to say specifically about circumstances where risk and internal audit are combined?

Across our membership there is a range of independence levels between the lines of defence and this will only widen as the scope of the Code increases. In general we do see broad separation between risk and IA however this will be highly dependent on the organisation, its structure and risks. In instances where there may be overlap between risk and compliance functions, appropriate checks and balances should be in place to ensure independence is maintained. There is a danger that if the Code is too prescriptive in certain areas this could limit usage and therefore we propose that the code remains open and flexible so that the AC can determine how best to structure IA to make it as effective, efficient and high quality as possible.

3) Should internal audit have the right to attend and observe Executive Committee meetings?

Do you agree that we should now raise the bar for the profession and insist that internal audit have a seat at the table at the Executive Committee?

We believe IA should have the right to attend executive committee meetings however it should be at the discretion of the executive and AC to exercise this. It is of utmost importance that their independence and challenge is not compromised if they do attend these. We therefore propose that the Code reflects this flexibility and does not prescribe that IA must attend these meetings.

From a practical perspective, there are a number of concerns we have with this proposal. Firstly, we question whether IA attending the executive would affect their independence. Furthermore the proposal that IA also review the information presented to the board and executive management, would cause a conflict of interest if IA also attended the meetings. As drafted, the Code is unclear as to what the breadth of this information for review by IA would be. If proposed, the Code should be more specific using risk bases to determine what information IA may need to

review. We also query whether IA would have the time and resources to perform this work whilst also attending the meetings.

5) Should the secondary executive reporting line be to the CEO, or should we adopt a more flexible approach in the new Code?

In the majority of organisations spanning all sectors there is a formal reporting line to the Audit Committee via the Audit Committee Chair.

However, whilst a secondary reporting line to the CEO is now common practice in the financial services sector, for other organisations it is often the case that they will have a secondary reporting line to another member of the executive management team such as the CFO.

In promoting internal audit best practice and in raising the bar across the profession, should we provide clear guidance that the secondary reporting line should be to the CEO? Or should we adopt a more flexible approach? If we adopt a more flexible approach, how do we mitigate the risk of potential conflicts of interest that could arise from a secondary reporting line (e.g. to the CFO)? As an alternative to a secondary reporting line to the CEO, would it be acceptable to have a secondary reporting line to another member of the executive management team?

The current structure of secondary reporting line varies across our membership. We believe this is advantageous, as companies can select a reporting line most appropriate for their IA needs. We therefore believe it's more beneficial for flexibility to be retained in this area, rather than prescribing the secondary reporting executive automatically being the CEO.

If the reporting line goes outside the CEO, the organisation would need to have in place safeguards to ensure that any matters relating to that reporting line are raised to a different executive, which should be at the discretion of the AC to decide.