

Chartered Institute of Internal Auditors
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11 October 2019

By email: iiapolicy@iia.org.uk

Dear Sir or Madam

Consultation on Internal Audit Code of Practice

Introduction

As Audit Committee Chairs, we have a keen interest in having a robust and effective internal audit function and there is much in this draft Code of Practice which we support and that cannot be argued with. So that the Code is taken seriously, it's important to recognise that there will be different models applied in order to satisfy the key principles. It needs to be recognised that it will not be appropriate for many companies to hire the level of internal audit head envisaged in the code. It needs to be left to the judgement of the Audit Committee Chair to approve the resourcing model that a particular business requires. These are set out below. In the Appendix we provide answers to the consultation questions.

ACCIF key discussion points

We do not believe that the draft Code acknowledges sufficiently the large variation in size and nature of internal audit functions across the listed, private and third sector markets. This is not a level playing field and for many companies the standards envisaged by the Code of Practice represent a very significant step up from where we are at present. Whilst the ambition to provide an industry benchmark for best practice internal audit is laudable, we do not believe it would be practicable for many FTSE 250 companies to implement and comply with several of the specific organisational and process aspects of the Code, such as the seniority of the head of internal audit and meaningful reviews of key corporate events such as those identified in paragraph 6e. We are concerned that the inclusion in the Code of rules which are not practicable for companies with small internal audit functions could result in a new expectation gap. They need to be fit for purpose in profile, staffing and competence.

In our view the Code would benefit from being more principles-based focusing on the core disciplines for any internal audit function of unrestricted scope, independence and reporting. On the basis of those principles, audit committees should then be able to make their own judgements, on a company by company basis, on the areas they would like assurance over and the amount of resource which is required. To drive transparency of the operation of this judgement by the audit committee, the Code could encourage audit committee chairs to report on how they ensured that the principles were being met including some examples of particular activities.

A key driver of the effectiveness of internal audit functions is the quality of the Head of Internal Audit. It comes down to the individual and the strength of their relationships within the business. The Audit Committee Chairman has an important role to play to see that the appropriate sponsorship for the head of internal audit is in place. Resourcing to meet the new Code of Practice is likely to be a significant challenge.

We would also suggest that consideration is given to the timing of the launch of the Code so that there is appropriate conformity with other reviews being undertaken at present, for example the Brydon review on the quality and effectiveness of audit.

Background on the ACCIF

Launched in October 2015, the ACCIF is an independent forum focused on FTSE 350 company audit committees. Its overall objective is to promote good governance by enhancing the leadership by audit committee chairs through the sharing of experiences and the establishment of best practice.

We would welcome the opportunity for a further discussion of these views with you. Please contact me (jocklennox@gmail.com) if you have any questions in relation to the comments made in this letter.

Yours sincerely



Jock Lennox
On behalf of the ACCIF board

Appendix

Consultation questions

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

As stated in our covering letter, an area of concern at present is that the draft Code does not acknowledge the large variation in size and nature of internal audit functions across the listed, private and third sector markets. This is by no means a level playing field and for the vast majority of companies the standards envisaged by the Code of Practice represent a significant step up from where we are at present.

The organisational and process aspects of the draft Code of Practice are in a number of respects too prescriptive such that we do not believe the Code will in practice be capable of being applied by many FTSE 250 companies that have an internal audit function. In our view the Code should be more principles-based focusing on the core disciplines for any internal audit function of unrestricted scope, independence and reporting. On the basis of those principles, audit committees should then be able to make their own judgements, on a company by company basis, on the areas they would like assurance over and the amount of resource which is required.

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

As noted above, we do not believe it is appropriate to assume a 'one-size-fits-all' approach to internal audit. Different organisations will have different risk and assurance frameworks which reflect the nature of their business. We believe that the Code Practice should be principles-based so that organisations can apply the Code in a proportionate and practical manner.

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

We believe that internal audit should have the right to attend Executive Committee meetings to enable them to obtain greater insight into senior management's risk and control consciousness. However, we do not believe that it is practicable for companies other than very large groups to recruit and retain heads of internal audit with the level of business and management experience necessary to give them the appropriate standing, access and authority to challenge the executive.

4. Should the new Code include guidance and best practice on the outsourcing of internal audit provision?

The Code should focus on the core principles of an effective internal audit function. Then, if an organisation chooses to outsource its internal audit provision, the same principles should apply with no distinction necessary for outsourced functions.

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

In line with our responses above and the comments in our covering letter, we believe there should be a more flexible approach in the Code. We agree that it is important that the internal audit function has an executive level 'sponsor' but it will not always be appropriate for this to be the CEO – sometimes it could be the CFO or even the General Counsel. It will really depend on the risk and assurance framework within the organisation. It is the job of the chair of the audit committee to ensure that internal audit's independence and objectivity is not impaired in any way by their secondary reporting line.

6. Should the new Code include guidance on how an internal audit function may provide assurance services where it had previously performed consulting services?

We believe that this represents another area where there needs to be more acknowledgement of the differences between companies' risk and assurance frameworks. In smaller companies, internal audit will often be used to provide consulting services and this is an important resource for the organisation. Principles in the Code should be sufficient to safeguard against the risk of internal audit "marking their own homework".

7. Are there any other matters which should be addressed in the Internal Audit Code of Practice?

See the comments in our covering letter. We would also note that paragraphs 9 and 10 of the draft Code seem very laboured and complex by comparison with the rest of the Code, and in our view they should be greatly simplified and shortened. For example, separate functions such as risk management and compliance rarely exist in smaller listed companies outside regulated sectors.