
III. MODEL DOCUMENT: INTERNAL AUDIT DEPARTMENT CHARTER

**ADOPTED
BY THE AUDIT COMMITTEE
OF THE COMPANY “ _____ ”
MEETING MINUTES
No _____
OF _____ 20__**

SIGNATURE OF THE CHAIRPERSON OF AUDIT COMMITTEE

DATED THIS __ DAY OF _____, 20__

Approved
by the Board of Directors
of the “[NAME OF THE COMPANY]”
No _____
of _____ 20__

Signature of the Chairperson of the Board of Directors

Dates this __ day of _____, 20__

Signature of the Chief Executive Officer

dated this __ day of _____, 20__

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Color Coding Conventions:

Black colored provisions:	Minimum acceptable provisions which are considered minimum requirements that the organization should be in compliance with.
Green colored provisions:	Better provisions which represent further steps to strengthen internal controls in the organization.
Blue colored provisions:	Desirable provisions which indicate that the organization has more mature corporate governance and a more established internal control system.
Red colored provisions:	Best practice provisions which indicate that the organization aspires to conform to the highest international internal controls practices.

1. GENERAL PROVISION

- 1.1. The Internal Audit Department (IAD) is an internal function set up to provide independent assurance on internal controls put in place by management on the business processes to detect specific risks and prevent them from happening. Internal audit is considered an integral part of the Company's Risk Management Framework.
- 1.2. This Charter defines the mission, scope of work, organization, accountability, authority and responsibilities of the IAD of the Company. It governs how the Chief Internal Auditor and other staff of the department discharge their duties and conduct internal audit activities within the overall Risk Management Framework and Internal Control System of the Company.

2. DEFINITIONS

- 2.1. For the purposes of this Charter, the terms used as follows shall have the following meanings:
 - 2.1.1 Chief Internal Auditor - the most senior executive responsible for Internal Audit of the Company. Similar titles may include Director of Internal Audit or Head of Internal Audit. The position reports functionally to the Audit Committee of the Board and with a dotted line to the Chief Executive Officer administratively.
 - 2.1.2 Enterprise Risk Management - a process, effected by the Board of directors, Management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and to manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives.
 - 2.1.3 External Audit - a periodic examination of the books of account and records of an entity carried out by an independent third party (the auditor), to ensure that they have been properly maintained, are accurate and comply with established concepts, principles, accounting standards, legal requirements and give a accurate and fair view of the financial state of the entity.
 - 2.1.4 Framework for Objectivity Management - describes the framework based on which a professional manage objectivity when discharging of the duties. In the profession of Internal Audit, the IIA published such a framework, namely, Independence and Objectivity: A Framework for

Internal Auditors in 2001.

- 2.1.5 Internal Audit
 - 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.
- 2.1.6 Internal Audit Activities
 - referred to below also as “audit activities”, provides independent assurance to the Board of Directors and senior management on the quality of effectiveness of the Company’s internal control, risk management and governance systems and process, thereby helping the board and senior management protect the Company and its reputation.
- 2.1.7 Internal Control
 - a process, effected by an entity’s board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in (i) effectiveness and efficiency of operations; (ii) reliability of financial reporting; (iii) compliance with applicable laws and regulations.
- 2.1.8 Internal Control System
 - consists of all the procedures, methods and measures instituted by the Board of Directors and management to ensure that operational activities progress in a proper fashion.
- 2.1.9 Non-audit activities
 - The following three types of activities undertaken by IAD staff, in line with this Charter: quality assurance activities (in monitoring and assessing on-going projects whether project objectives are reasonable and would be achieved); consulting services and trainings (in providing assistance and training to organization’s staff in designing management accountability systems and reengineering operations); and control self-assessment facilitation (in supporting organization’s employees in holding structured discussions on how to achieve objectives in most efficient and effective way).
- 2.1.10 Risk
 - anything that can keep an enterprise from meeting its objectives.

- 2.1.11 Risk Assessment - process of identifying the risks to an institution, assessing the critical functions necessary for an institution to continue its business operations, defining the controls in place to reduce organization exposure and evaluating the cost for such controls. Risk analysis often involves an evaluation of the probabilities of a particular event.
- 2.1.12 Risk Management - coordinated activities to direct and control an organization with regard to risk.
- 2.1.13 Risk Management Framework - the complete set of components that provide the foundations and organizational arrangements for designing, implementing, monitoring, reviewing and continually improving Risk Management throughout the organization.
- 2.1.14 Risk Management Policy - a statement of the overall intentions and direction of an organization related to risk management.
- 2.1.15 Third Line of Defense - the third pillar within the three lines of defense¹ of an Enterprise Risk Management Framework formed by the Audit Committee and the Internal Audit function to provide independent assurance of an organization's Internal Controls and Risk Management Systems.

3. PURPOSE AND SCOPE OF WORK OF THE INTERNAL AUDIT DEPARTMENT

- 3.1. The purpose of Internal Audit is to provide independent, objective assurance **and consulting services** designed to add value and improve the organization's operations. It helps the organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of internal controls, **risk management, and governance** processes. The scope of work of the IAD shall cover all internal and outsourced business processes of the company. **Together with the Audit Committee to whom it reports, they constitute the Third line of Defense.**
- 3.2. By definition, Internal Audit is concerned with the historical performance of the Company with focus on the following:
 - 3.2.1. Effectiveness and efficiency of operations;

¹ Refer the description of the three lines of defense in the IFC Risk Management Committee Model Charter

- 3.2.2. Reliability of financial reporting in terms of timeliness and accuracy; and
- 3.2.3. Compliance with applicable laws and regulations.
- 3.3. Through independent checking and reviews, the IAD is to ensure that management has put in place appropriate Internal Controls to address business risks and to ensure that such controls are adequately functioned. Quality and continuous improvement are fostered in the organization's control process
- 3.4. Opportunities for improving management control, profitability, and efficiency may be identified during audits. They will be communicated to the appropriate level of management.
- 3.5. As the Board of Directors has ultimate responsibility over the Company's Internal Control Systems, the IAD shall provide assurance to the Board the proper function of such Internal Control Systems. The Internal Audit Activities therefore is an integral part of the monitoring function of the Board in the Corporate Governance framework.

4. ACCOUNTABILITY

- 4.1. The IAD is a unit within the Company with a strong degree of independence. The IAD is a separate budget center and operates independently of the business units whose internal controls and business activities it reviews.
- 4.2. The IAD shall be accountable to the Board to discharge its duties of:
 - 4.2.1. Assessing the adequacy and effectiveness of the Company's processes in controlling its activities and managing its risks;
 - 4.2.2. Identifying and reporting weaknesses / issues related to those processes that might compromise controls, and recommending improvements / rectifications; and
 - 4.2.3. Coordinating with other control and monitoring functions (Risk Management, compliance, security, legal, ethics, environmental, External audit).
- 4.3. The IAD reports to the Chief Internal Auditor and is ultimately accountable to the Audit Committee on coordinating the effective and efficient running of the Company's Internal Audit Function.
- 4.4. The Chief Internal Auditor shall be a senior executive of the organization (but not necessary part of the senior management team). Appointment and dismissal of the Chief Internal Auditor shall be approved by the Audit Committee.

4.5. The IAD, through the Chief Internal Auditor, shall have direct access to management and the Board. The Board and senior management shall give the IAD the necessary support. Issues raised by the Internal Auditors shall receive the necessary attention from the Board, the Audit Committee, senior management and business units.

5. AUTHORITY

5.1. The IAD shall be independent of the day-to-day operations of the business and have freedom to set its agenda, strategy and plan, within the remit and scope of work set for the function. Chief Internal Auditor and staff of the IAD shall have the authority to:

5.1.1. Have unrestricted access to all functions, records, property, and personnel;

5.1.2. Set its strategy, audit focus, annual plan, methodology, and resource plan, within the remit and scope set for the department;

5.1.3. Have full and free access to the Audit Committee; and

5.1.4. Obtain expert services or additional resources in performing its duties.

5.2. They however shall not:

5.2.1. Perform any day-to-day operational duties for the Company;

5.2.2. Be involved in any decision making beyond those related to the Internal Audit function;

5.2.3. Have approval authority on transactions other than those directly related to internal audit activities; and

5.2.4. Manage staff other than those under the IAD, except to the extent that such staff have been assigned to assist in the department's activities.

6. INDEPENDENCE AND OBJECTIVITY

6.1. To maintain independence, the IAD and its staff shall not have any operational responsibilities and be involved in any operational decision-making. Remuneration of the internal auditors, including the Chief Internal Auditor, will not be linked to business performance of particular business lines, but would be determined in accordance with the remuneration policies and practices of the Company, and would be approved by the Audit Committee.

6.2. The IAD shall be independent of management in planning its audit activities.

- 6.3. It shall have a separate budget independent of the operating departments. This internal audit budget, and the related resource plan will be approved by the Audit Committee.
- 6.4. Individual objectivity of the internal auditors is maintained through impartiality, unbiased attitude and avoidance of conflict of interests, which are integrated into a Framework for Objectivity Management, which will include at minimum: identification of threat to objectivity, assess significance of threat, identify mitigating factors, assessing residual threats, proactive management of residual threats, assessing presence of unresolved threats to objectivity, reporting, ex-post review and monitoring
- 6.5. In exceptional cases, an IAD staff member could accept a non-audit engagement identified as one that could potentially threaten the IAD staff member's independence and/or objectivity vis-a-vis future assurance engagements, if and only if, pre-approved by the Chief Internal Auditor (with Audit Committee consent), who would be obligated to consideration the costs and benefits of such an engagement. Any such engagement shall be adequately documented and reported to the Audit Committee in writing.²
- 6.6. Only the Audit Committee may require IAD staff to accept consulting engagements that have been identified by Chief Internal Auditor to fall into the scope of section 6.5. above. When IAD staff are requested by the Audit Committee to conduct engagements that are determined by the Chief Internal Auditor to fall into section 6.5 above:
 - 6.6.1. Before the start of the consulting engagement, the Chief Internal Auditor will communicate in writing with the Audit Committee that the requested engagement will impair independence or objectivity, describe the nature of impairment, indicating the consequences of the impairment for future audit engagements, and request a response in writing from the Audit Committee; and
 - 6.6.2. If the Audit Committee directs the IAD staff to proceed with the engagement in question, the Chief Internal Auditor will document the impairment in the consulting audit engagement's documentation and the Internal Audit Annual Plan.

7. ORGANIZATION

² An example of a non-audit engagement could be a "consultancy" assignment to review and recommend improvements of a certain function that is not within the immediate audit plan scope of IAD, but could be in the future. Should said function eventually be subject to internal audit, the Chief Internal Auditor would need to consider the past engagement and assign auditors who did not take part in the referenced engagement, to the extent possible.

- 7.1. The IAD is a corporate function headed by the Chief Internal Auditor (similar titles include Head of Internal Audit, Director of Internal Audit). It shall be sufficiently staffed to perform its duties.
 - 7.2. If the Company has subsidiaries, internal audit should cover the subsidiaries as well. Depending on the size and nature of business of the subsidiaries, they could either be covered by a corporate internal audit function or have a separate individual audit department set up. The group level IAD shall assume a coordinating role to ensure consistency in standards and practices.
 - 7.3. The CIA, who reports functionally to the Audit Committee and administratively to the Chief Executive Officer, is responsible for and held accountable to the execution of the Annual Internal Audit Program in the Company. Specifically, the CIA is responsible to:
 - 7.3.1. Conduct internal control evaluation and Risk Assessment to identify internal control weaknesses and risk areas that might prevent the Company from achieving its objectives;
 - 7.3.2. Develop a risk-based annual audit plan and manage the implementation of the plan;
 - 7.3.3. Review the operations and financial systems of the Company to ensure reliability of financial reporting, compliance of rules and regulations and improvement of efficiency and effectiveness of operations;
 - 7.3.4. Provide leadership to and manage the development of staff of the IAD; and
 - 7.3.5. Manage the resources of the IAD in the most efficient and effective manner.
- A model job description of the CIA can be found in Annex 1.
- 7.4. Resources
 - 7.4.1. The IAD shall be staffed with full time staff who will perform the engagements with proficiency and due professional care. Internal auditors will possess the knowledge, skills and other competences needed to perform their individual responsibility and the internal audit function as a whole will collectively possess or obtain the knowledge, skills and other competences needed to undertake Internal Audit activities. **The IAD shall have, and/or would be able to access adequate resources to undertake the Annual audit plan approved by the Audit Committee.**
 - 7.4.2. **The Internal Audit staff in the function should be knowledgeable about the Company's business and operations. Senior members of the department shall have direct operational experience in the industry the Company is involved in to enable them to have a good understanding of where risks lie,**

where weaknesses are usually found and where internal controls should be set. The Internal Audit staff shall possess the relevant professional qualifications such as recognized professional certification of one of the recognized professional accounting bodies, or Certified Internal Auditor of the Institute of Internal Auditors, FCA, and ACCA.

- 7.4.3. Staff of the IAD shall include competent individuals who have the financial accounting and reporting knowledge. They should be familiar with the relevant standards and regulations related to financial reporting and internal controls in all jurisdictions in which the Company operates. Familiarity with the relevant international standards in financial reporting and internal audit, such as the International Financial Reporting Standards (IFRS), the International Standards in Professional Practice of Internal Auditing respectively are added advantages. The IAD as a whole shall also be knowledgeable about the international standards in external auditing and the audit process.
- 7.4.4. Staff of the IAD shall have some knowledge of the risk assessment process and the compilation of the Risk Register managed by the Risk Management Department as they shall provide input in risk identification and development of risk control measures, as well as assurance on functioning of those control measures. Knowledge of Enterprise Risk Management is an added attribute.
- 7.4.5. The IAD shall also include compliance and IT professionals who have the knowledge and experience to carry out compliance and IT audits respectively. There shall also be legal professionals in the team who have the legal background to understand the legal implications of the business practices. They shall be familiar with the relevant international standards and practices.
- 7.4.6. Staff of the IAD shall be provided with the on-going technical training in Internal Audit. Training on soft skills to deal with people and processes shall be provided. Resources shall also be provided to enable members of the team to gain the relevant professional qualifications.

7.5. Personal Attributes of the IAD staff

- 7.5.1. Members of the IAD shall possess the personal attributes of honesty, integrity and high degree of ethical standard. Being objective, independent and competent are also basic attributes³. They shall also be familiar with the prevailing accounting and financial reporting standards of the jurisdictions in which the Company operates. They are expected to

³ As stated in the IIA Code of Ethics

have a strong sense of compliance and are familiar with the relevant legislations and rules of the jurisdictions in which the Company operates.

7.5.2. They shall strive to be independent and are prepared to assess themselves. They shall have an inquisitive mind to identify internal control weaknesses in operations, and the necessary quantitative and analytical skills to assess and analyze them.

7.5.3. They shall have the interpersonal and communication skills to work with management and business units while having the assertiveness and resolute to challenge them on non-compliant or even fraudulent issues.

7.5.4. Given the risk landscape continues to evolve and change, they shall have an open mind and be willing to change.

8. RESPONSIBILITIES

8.1. Under the leadership of the Chief Internal Auditor, the department has the responsibilities to:

8.1.1. Develop a flexible annual risk based audit plan using an appropriate risk-based methodology, including any risks or control concerns identified by the Board and management, related to all in-house and outsourced business processes, and submit that plan to the Audit Committee for review and approval as well as periodic updates;

8.1.2. Implement the approved annual audit plan;

8.1.3. Carry out internal auditing tasks including, but not limited to, compliance checks against internal policies and procedures as well as applicable external rules and regulations; reliability checks of timeliness and accuracy of financial transactions and reporting; and assurance of effectiveness and efficiency of business operations; and as appropriate any special tasks or projects requested by the Audit Committee and management;

8.1.4. Issue periodic reports to [management / Audit Committee] reporting results of audit activities, issues found and recommendations;

8.1.5. Maintain and develop a team of professional audit staff with sufficient knowledge, skills, experience, and professional qualifications to meet the requirements of this Charter;

8.1.6. Ensure internal staff have relevant training and development opportunities;

- 8.1.7. Assist in the investigation of suspected fraudulent activities within the Company and notify [management / Audit Committee] of the results;
- 8.1.8. Consider and advise the Audit Committee on the scope of work of the external auditors and regulators, as appropriate, for the purpose of providing optimal audit coverage to the Company at a reasonable overall cost;
- 8.1.9. Keep the Audit Committee informed of emerging trends and successful practices in internal auditing;
- 8.1.10. Evaluate and assess independently, from the internal control and risk perspectives, significant organization, process, systems and policy changes that are incidental to the growth and expansion of the Company (such as introduction of new products or services, merger and acquisition), working with the Risk Management and Compliance Department in the process;
- 8.1.11. Work with the Risk Management Department in identifying control weaknesses against strategic and operational risks, recommending enhancement of existing control measures / development of new control measures, and monitoring the effectiveness of those measures; and
- 8.1.12. Provide input in the development and update of the Company's Risk Management Policy and Risk Register in light of risks identified during the conduct of internal audit activities.

9. INTERNAL AUDIT PROCESS

- 9.1. The Chief Internal Auditor and his/her staff shall regularly review the Company's written policies and procedures, particularly the internal controls embedded in them. They shall also regularly update their understanding of the major business processes of the Company in order to have a good understanding of the risks and inefficiency inherent in the processes. An audit universe, a list of all auditable entities, shall be compiled.
- 9.2. At least annually, the Chief Internal Auditor will submit to the Audit Committee senior an annual internal audit plan for review and approval. The internal audit plan will consist of a schedule of audit assignments as well as budget and resource requirements for the next fiscal/calendar year.
- 9.3. The internal audit plan will be formulated using a risk-based approach whereby audit assignments are selected and prioritized through a risk assessment exercise. Input from senior management and the Board will be taken into account but the Chief Internal Auditor shall have freedom to develop the plan. Any significant deviation from the approved internal audit plan will be communicated to the Audit Committee through periodic reports.

- 9.4. A written report will be prepared and issued on completion of each internal audit engagement and will be distributed as appropriate. Internal audit results will also be communicated to the Board of Director, via the Audit Committee.
- 9.5. The internal audit report shall include findings and recommendations, and may include management's response and corrective action taken or to be taken. The Chief Internal Auditor shall agree with management a timetable for implementing corrective actions. The Internal Audit team will follow-up according to the timetable. All significant findings will remain in an open issues file until cleared.

10. RELATIONSHIP WITH MANAGEMENT AND RISK MANAGEMENT DEPARTMENT

- 10.1. Management is responsible to ensure an internal control system is in place. The IAD provides independent assurance to the Board that such internal control system is functioning as intended and recommend internal control enhancements if weaknesses are found and/or to comply with the latest rules and regulations.
- 10.2. The Risk Management Department is responsible for coordinating Risk Assessment and updating the Risk Register periodically. IAD will make use of the assessment findings to formulate the audit plan.
- 10.3. Internal Audit is responsible for providing independent assurance on internal controls put in place by management on the business processes to detect specific risks and prevent them from happening. IAD therefore is a key component of the Company's Risk Management Framework. It shall work with the Risk Management Department to determine appropriate control measure to address a risk identified and periodically check to ensure the control measure is effective.

11. PROFESSIONAL STANDARDS

- 11.1. The IAD shall adhere to the professional standards required by law or regulation in the jurisdictions in which the Company operates.
- 11.2. The IAD shall follow the relevant international standards in Internal Controls.
- 11.3. Staff of the IAD shall follow the standards and code of ethics stipulated by the recognized professional organizations, such as the Institute of Internal Auditors (IIA). The internal audit activity will meet or exceed the Standards for the Professional Practice of Internal Auditing of The IIA.

12. EVALUATIONS

- 12.1. [The Charter shall be subject to periodic review as needed. / The Chief Internal Auditor shall develop and maintain a Quality Assurance and Improvement Program, to assess whether the purpose, scope, accountability, and responsibilities, as defined in this Charter, continue to be adequate to enable the IAD to accomplish its objectives. This Program will include at least annual internal

assessments and external assessments, undertaken by qualified independent assessor from outside the organization at least once every five years. The result of these periodic assessments is to be communicated to senior management and the Board of Director via the Audit Committee.]

ANNEX 1: SAMPLE JOB DESCRIPTION OF THE CHIEF INTERNAL AUDITOR

POSITION TITLE: **Chief Internal Auditor**

Reporting to: Chief Executive Officer⁴ / Chairperson of the Audit Committee, with dotted line to the Chief Executive Officer administratively

Role Purpose: Strategic leadership of the Internal Audit function. Providing independent assurance that effective and efficient internal control system is in place to manage risks that might prevent the Company from achieving its business objectives.

Main Responsibilities

- Plan and conduct audits to assess controls, operational efficiencies and compliance with selected policies, procedures and regulations. Resolve audit problems that occur and develop modifications to coverage and schedule.
- Ensure work papers are adequately documented and audit evidence is sufficient.
- Prepare accurate audit reports for CEO and Audit Committee.
- Assist in developing annual audit plan and submit to CEO and Audit Committee for review and approval.
- Establish policies and procedures to guide internal audit function.
- Supervise and guide staff in support of the Company's mission and audit initiatives.
- Elicit information from knowledgeable internal/external sources about areas and functions to determine appropriate audit direction/methodology. Research all pertinent data (law, current issues, work papers, reports). Develops reasonable budgeted hours.
- Research and keep abreast of legislative issues, new audit regulations/trends and audit methodology.
- Conduct periodic training workshops to promote awareness of internal controls and to discuss changes in policies that will impact the system flow of information.
- Share information and coordinate activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimize duplication

⁴ Only in the rare occasion that the company does not have a Board of Director. Reporting to the Chairman of the Audit Committee is considered a minimum requirement.

of efforts.

- Discuss updates of new internal controls and internal audit standards, trends and regulations with Audit Committee, management and relevant staff.
- Assist external auditors as appropriate; assist in coordinating the Company's response to audit findings and recommendations.
- Participate in various working groups or task forces tasked with policy/procedure development and operational improvements.

Requirements

- Degree-holder in finance, accounting, law or related disciplines.
- Minimum 15 years of relevant working experience in accounting, compliance and/or internal audit, preferably with exposure to the industries in which the Company operates.
- A high degree of professional and ethical standards.
- A certified auditor and member of a recognized body such as IIA.
- A qualified accountant and member of a recognized accounting body such as HKICPA, ACA, ACCA, CIMA, AICPA etc.
- Additional qualifications including CIA and Certified Fraud Examiner would be desirable
- Proven track record in leading the internal audit function in sizeable organizations.

Core Competencies

- A sound understanding of Internal Control principles and philosophy.
- A sound understanding of accounting and financial reporting standards of the jurisdictions in which the Company operates.
- A broad understanding of the operations and products of the Company.
- Ability to effectively analyze operations and processes, and identify internal control weaknesses or inefficiency, and provide solutions.
- Professional integrity to remain independent when conducting him/herself.
- Ability to communicate and work with people at different levels and from different background.

- A keen and effective team player with excellent inter-personal skills.
- Ability to understand and interpret financial information and principles.
- In-depth knowledge of international standards and methodology of Internal Audit.
- Excellent project management skills.
- Ability to think strategically.
- Ability to motivate and influence others, including those who are in more senior positions.
- Sound understanding of Enterprise Risk Management methodologies and how it complements Internal Audit