

March 2, 2012

Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel, Switzerland

Response e-mailed to baselcommittee@bis.org

RE: Response to the Basel Committee on Banking Supervision – Consultative Document – “*The Internal Audit Function in Banks*”

Dear Sir/Madam:

The Institute of Internal Auditors (IIA) appreciates the opportunity to provide comments on the consultative document entitled “The internal audit function in banks” from December 2011. We collaborated with a number of internal audit thought leaders globally in developing our comments. Our comments are based on discussions conducted by a core team of internal audit professionals who serve on The IIA’s Professional Issues Committee. These professionals consist of Chartered Accountants, Certified Public Accountants, and Certified Internal Auditors who have worked in the public and private sectors, internal and external auditing, and small, medium, and large domestic and multinational companies.

Over the last decade, the banking industry has undergone major changes as did the audit profession. Therefore, we applaud the issuance of a revised supervisory guidance for assessing the effectiveness of the internal audit functions in banks as an effort to replace the 2001 document “Internal audit in banks and the supervisor’s relationship with auditors.”

The following are our principal comments and observations:

Principle 7 of the document appears to restrict the overall responsibilities of the internal audit function. With regard to its assurance role to the board, the internal audit function is meant to provide global assurance to the board on the internal control and risk management systems pertaining to all governance objectives. This encompasses business control objectives, financial reliability, regulatory and legal compliance, etc.

We recommend inclusion of stricter language pertaining to the independent review of the internal audit function, as covered in the document under “Responsibilities of the board of directors and senior management.” The Standard 1300 of the International Standards issued by The IIA requires a “Quality Assurance and Improvement Program”, also 1311 requires internal assessments including ongoing monitoring and periodic assessments and, 1312 requires external assessments must be conducted at least once every five years. We recommend including a reference to periodic independent review of internal audit functions, including reference to Standards 1300, 1311 and 1312 in paragraph 43 of the document.

Regarding the Overview section “Principles relating to the supervisory expectations relevant to the internal audit function”, we suggest highlighting the importance of internal auditors acting with integrity and in accordance with The IIA Code of Ethics and the International Standards for the Professional Practice of Internal Auditing.

Relative to the described responsibilities of the board of directors and senior management (section A 5), we believe senior management should keep the internal audit function not only informed of new developments, initiatives, projects, products and operational changes, but of changes in strategic direction, as well.

We recommend including the following aspects within the list of minimum requirements for an internal audit charter (section A 4):

- Provide information about evolving models on governance, risk, control and compliance (GRCC) to board members and promote education of bank personnel on GRCC to ensure awareness and importance.
- Attend the bank’s governance committee meetings to provide advice and counsel. In order to maintain its independence, internal audit should act as an advisor and not have responsibility for the committee’s work.
- Perform and report on fraud analysis and conduct special verification of potential irregularities.

We recommend replacing paragraph 29 as follows:

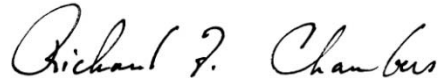
The head of internal audit is responsible for developing an annual risk-based internal audit plan that can be part of a multi-year plan. The head of internal audit takes into account audit risk factors as well as the bank’s risk organizational objectives and risk management framework, including using risk appetite levels set by management for the different activities or parts of the organization. If the framework does not exist, the head of internal audit will consider perceived risks on the basis of consultation with senior management. The board’s approval of the audit plan implies that an appropriate budget will be available to support the internal audit function’s activities. The budget should be sufficiently flexible to adapt to variations in the internal audit plan in response to changes in the bank’s risk profile.

Principle 17 paragraph 83 lists several criteria related to the assessment of the internal audit function based on supervisory expectations as set out in section A of the guidance. We recommend including performance measures or benchmarks, such as The IIA’s *International Professional Practices Framework* (IPPF), which the supervisory authority might use to evaluate whether the internal audit function is inadequate or ineffective.

As a general comment, we suggest reassessing the design of the document. The numbering system is complex and complicates the understanding of the document.

The IIA welcomes the opportunity to discuss any and all of these recommendations with you. We wish to reiterate that we consider the issuance of this consultative document both timely and highly worthwhile. We offer our assistance to the Basel Committee in the continued development of this guidance.

Best Regards,

A handwritten signature in black ink that reads "Richard F. Chambers". The signature is written in a cursive, flowing style.

Richard F. Chambers, CIA, CGAP, CCSA, CRMA
President and Chief Executive Officer

About The Institute of Internal Auditors -

The IIA is the global voice, acknowledged leader, principal educator, and recognized authority of the internal audit profession and maintains the International Standards for the Professional Practice of Internal Auditing (Standards). These principles-based standards are recognized globally and are available in 29 languages. The IIA represents more than 170,000 members across the globe and has 105 Institutes in 165 countries that serve members at the local level.