

28 April 2025

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Australian Securities and Investments Commission
Level 5
100 Market Street
Sydney NSW 2000

Dear ██████████

RE: DP Australia's evolving capital markets: A discussion paper on the dynamics between public and private markets

We refer to the release of the discussion paper on Australia's evolving capital markets and thank you for this valuable work and invitation to comment.

Capital Markets Enhanced by Competent Governance

The three lines model and Principle 4 (oversight) of ISO 37000:2021 'Governance of organizations — Guidance' emphasise that competent governance does not rely on a single stream of information. Essentially those running the organisation must be well informed about its operation and independent sources of information help ensure that decisions are not biased towards short term management objectives.

Further, governance is more than simple fiduciary duty to beneficiaries. It is well accepted that governance includes retaining social license to operate. To do this successfully, those who govern the organisation need to be fully informed of its activities and the consequences of those activities.

Having an effective internal audit function will provide an independent stream of information about the operation of an organisation to those charged with its governance.

Internal Audit, Standards and Good Governance

The Institute of Internal Auditors-Australia is the professional body for internal auditor. The work of internal auditors, when delivered in adherence to and organisational support for the Global Internal Audit Standards (GIAS) has enhances organisational performance, especially in evolving regulatory landscapes and emerging risk environments¹.

Internal audit is recognised by ASIC as an important element in the control environment of organisations that can contribute to more effective risk management. Because of the benefits it affords in effective governance, the ASX Corporate Governance Principles and Recommendations 4th Edition require a listed entity to have an internal audit function, and if they do not, the organisation is required to explain why they do not and in internal audits absence, how risk management and internal control processes are managed, evaluated and continuously improved upon².

¹ <https://www.nature.com/articles/s41599-024-03835-3#Sec1>

² <https://asic.gov.au/regulatory-resources/financial-reporting-and-audit/auditors/internal-audit/>

The 5th edition draft went further, recognising the correlation between adherence to the GIAS and good corporate governance, and requiring listed entities to both have an internal audit function and comply with the GIAS (within its ‘if not, why not’ framework). Unfortunately, the draft 5th edition, despite its extensive public consultation phase was withdrawn by ASX because the Council responsible for it could not reach consensus on aspects related to diversity reporting. As a result, the governance enhancement of requiring internal audit functions to operate to standards including objectivity and public interest were not realised.

Internal Audit and External Audit

ASIC recognised the value of external auditors in protecting Australian investors - “Auditors play a critical role in ensuring that **Australian investors can be confident and informed when making investment decisions**. High-quality audits support the quality of financial reports and enable investors to rely on the auditor’s independent assessment of financial reports.”³

For effective and responsible financial market performance, in addition to external audit, APRA requires its regulated institutions to have “an independent and adequately resourced internal audit function for the institution... and that the objectives of the internal audit function must include evaluation of the adequacy and effectiveness of the financial and risk management framework of the institution”⁴.

There is a natural reliance on external audit as a means to provide investors assurance over an organisation’s past financial performance. While past financial performance shows the potential inherent financial strength of a company, it does not provide assurance on the overall risk management framework and broad range of internal controls (particularly non-financial), nor current practices and the organisational culture underpinning performance – this is the domain of internal audit.

Just as external audit enhances effective markets while protecting investors, we offer that internal audit applied in accordance with the Global Internal Audit Standards can likewise enhance effective markets while protecting investors by providing independent assurance over controls and risk management on a broader range of threats and opportunities.

Broad Adoption of the Three Lines Model

Good governance can be further enhanced in Australia by adopting the Three Lines Model which is a valuable example of how to bring about governance improvements for performance. At the heart of managing the challenging dynamics highlighted within the discussion paper, is the critical importance of effective risk management by organisations faced with multiple pressures.

We actively promote the Three Lines Model as a mechanism for establishing internal structures that support good governance. It allows for responsibilities regarding processes, controls and risk management to be clearly delineated between business areas. This Model should be further adopted by Australian entities (both public and private) to enhance their control environment and risk management and effectively utilise the independent third line of internal audit.

³ <https://asic.gov.au/regulatory-resources/financial-reporting-and-audit/auditors/audit-quality-the-role-of-directors-and-audit-committees/>

⁴ <https://handbook.apra.gov.au/standard/cps-510>

Conclusion and Recommendation

In reviewing the dynamics between public and private markets and the place of regulatory controls to protect investors, we believe the Australian public would be well served by increased requirements for entities to have an internal audit function that adhere to the Global Internal Audit Standards including the independence, objectivity and public interest requirements.

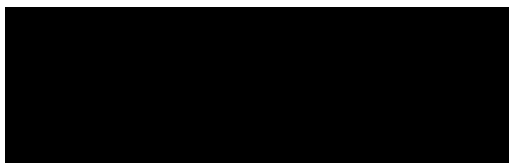
While it may seem to be administratively burdensome to mandate internal auditing or formal adoption of the three lines model, there is much to be gained by requiring all organisations that operate within the capital market to explain in a public report (or on their web site) the mechanisms that they have in place to ensure that those charged with their governance are not relying on a single source of internal information in their decision-making processes.

One low-regulatory burden mechanism for this could be the requirement for the inclusion in the Directors' declaration for audited financial statements to include a statement that the organisation has an internal audit function and that the function adheres to the Global Internal Audit Standards or, if not, why not. To be effective and reasonable, there would need to be some criteria to establish which entities would need to include this declaration – perhaps the ESG reporting thresholds could provide some guidance.

Such an action, would simply require organisations to share their governance framework and how those that govern assure themselves regarding the information upon which they make decisions – the decisions that affect the security of capital.

IIA-Australia would welcome the opportunity to discuss this and other related mechanisms to improve governance, the flow of capital and protecting investors' interests, including the Three Lines Model, the GIAS, and professional standing requirements of internal auditors.

Yours sincerely



Chief Executive Officer