IDB | Invest

INTERNAL AUDIT CHARTER

CORPORATE GOVERNANCE IMPLEMENTATION GUIDE

Corporate Governance

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About the Authors | **Cefeidas Group**

Cefeidas Group is an international advisory firm that helps clients achieve their goals in Latin America. Cefeidas has worked with the IDB and IDB Invest for over a decade. Cefeidas provides professional services in public policy, risk and strategy, corporate governance, stewardship and sustainability, and strategic intelligence and research. www.cefeidas.com

1. CORE PRINCIPLES OF THE INTERNAL AUDIT CHARTER

The Internal Audit is the independent assurance function that systematically assesses the effectiveness of the company's governance, risk management and internal control processes. It is the third line of defence of the control model and, when it operates with independence and real authority, it is one of the Board of Directors' most valuable allies in understanding what really goes on within the organisation.

The Internal Audit Charter — also referred to as the Internal Audit Statute or Internal Audit Regulations — is the formal document that establishes the mission, purpose, authority, scope, reporting lines, organisation, resources and responsibilities of the function. Without a Board-approved Charter, Internal Audit operates in a grey area: it may exist as an activity, but it lacks the institutional mandate that allows it to truly fulfil its role.

What the Internal Audit Charter is and is not

The Internal Audit Charter serves as the governance tool that formalises the existence and operation of the function. It is important to distinguish it from other related documents:

Internal Audit Charter	The institutional framework of the function: purpose, authority, independence, reporting lines, scope, responsibilities, resources and quality assurance. The document is approved by the Board.
Terms of Reference (ToR)	Operational descriptions of roles: of the Chief Internal Auditor and the department staff. These detail functions, profiles, operational authority and deliverables. They are set out in the Charter.
Annual Internal Audit Plan	The specific work schedule for the financial year, based on a risk assessment. It is prepared by the Chief Internal Auditor and approved by the Audit Committee (or the Board).
Internal Audit Manual	The team's daily methodologies, procedures, templates and working papers. It is operational, not governing.

Alignment with the Audit Committee Charter

The Audit Committee Charter establishes who oversees the function, while the Internal Audit Charter establishes how the function itself operates.

The Audit Committee is the governing body responsible for approving the Internal Audit Charter, receiving relevant reports, evaluating the Chief Internal Auditor and supervising the independence of the Internal Audit. Without a functional Audit Committee, the independence of the Internal Audit is compromised; without a robust Charter, the Audit Committee has no way to exercise its role effectively.

Download the Audit Committee Charter Implementation Guide here.

Why is an Internal Audit Charter essential?

Although it may seem like a mere bureaucratic formality, there are practical implications to having approved Charter in place that are felt from the very first day of operation. The Internal Audit function is structurally uncomfortable: by its nature, it must be able to review departments that report to the CEO and, on occasion, evaluate decisions of Senior Management itself. This is only possible when there is a written mandate approved at the highest level. The main reasons for regulating the function are as follows:

- **Institutional legitimacy.** The Charter constitutes the document through which the Board creates the function and empowers it with real authority. Without it, Internal Audit depends on the CEO and becomes another operational function, losing its value as an independent assurance.
- **Unrestricted access.** The Charter documents the auditor's right to access records, systems, personnel and facilities without restriction. This point is critical: without it, the auditor depends on the will of the party subject to audit.
- **Preserved independence.** It establishes the functional reporting line to the Audit Committee (not to the CEO or the CFO), stipulates that the auditor may not assume operational responsibilities, and prohibits linking the auditor's remuneration to the performance of the departments being audited.
- **Protection against pressure.** When a finding is uncomfortable, the Charter provides the basis on which the auditor can stand by their work. It is the difference between a team that objectively reports what it sees and one that reports what is convenient.
- **Clarity of expectations.** It defines what can be requested from the function, according to what timeframes and methodology. It avoids misaligned expectations between the Board, Senior Management and the function itself.
- **Trust from investors and funders.** Banks, investment funds and bond issuers consider the existence of Internal Audit Charter to be a key indicator of corporate governance maturity.

A frequent sign of trouble: medium-size and family businesses often have a function called "Internal Audit" that actually reports to the CEO or CFO, performs routine financial control tasks, and never reports to the Board. This is not Internal Audit; it is internal control in disguise. It is precisely the Charter that makes all the difference by establishing the auditor's remit and powers.

Scope and Application

The Charter applies to the Internal Audit function in its entirety, regardless of how it is organised operationally. This flexibility is deliberate: many medium-sized companies do not need (nor can they afford) an entire department, and the Charter should serve a single auditor as well as a team of several people.

Operating models covered by the Charter

Function performed by a single person (Chief Internal Auditor). This is the most common scenario in medium-sized companies. The Charter applies in full; what changes is the scope of coverage, not the requirements regarding independence and mandate.

Internal Audit function with several staff members. This allows greater specialisation in audits (financial, operational, IT, compliance). The Charter remains unchanged; the internal organisation of the department changes.

Fully outsourced function. The company hires an external firm to perform the function. The Charter remains necessary and continues to require approval of the Board: the thing that changes is the enforcer, not the mandate.

Mixed or co-sourced model. An in-house Chief Internal Auditor coordinates and oversees the work, whilst certain specialist audit tasks (cybersecurity, fraud, data) are outsourced to third parties.

Even a single person needs a Charter

The idea that a Charter is only "for large companies" is mistaken and dangerous. In fact, the smaller the function, the more critical the Charter, because there is no team to dilute the pressures on the auditor. A robust Charter provides a tool that allows a single auditor to defend their criteria against a CFO or CEO with greater seniority and organisational authority.

The Institute of Internal Auditors (IIA) explicitly recognises this fact and has published specific guidelines for small internal audit functions, emphasising that professional standards apply the same: the only thing that changes is how they are met, not whether they are met.

Purpose of the Charter

The Internal Audit Charter pursues five specific objectives:

- **To establish the mandate.** To formally define what the function does, its scope and what types of services it provides (assurance, consulting, research).
- **To ensure organisational independence.** Through functional reporting lines to the Audit Committee (or to the Board where no such committee exists) and the separation of all operational responsibilities.
- **To guarantee access.** To data, systems, records and people necessary to fulfil the mandate, without managerial restrictions or filters.

- **To establish accountability.** Frequency, content and recipients of reports, including escalation of significant matters.
- **To commit resources.** To ensure that the function will be provided with an adequate budget, staff and resources, and that any reduction in these requires justification to the Committee.

Advantages by type of company	
Family businesses	In family businesses, having an Internal Audit Regulation helps to separate the "family" dimension from the "company" dimension. It brings technical discipline to processes that may be overly personalised and reduces reliance on informal control based on personal trust. For family members who are not involved in management, it offers a guarantee that there is independent oversight of the management's actions. In succession processes or when new generations take over, robust regulations facilitate institutional continuity by making the oversight function explicit.
Growing medium-sized businesses	As the company grows, informal controls ("I know everyone and see everything") cease to be viable. The Charter allows the assurance function to be scaled up in an orderly manner, without having to wait for an adverse event to force it to be improvised. It is also one of the factors that institutional investors and banks take into account when assessing larger lines of credit: having a formalised internal audit function improves the perception of risk and, in some cases, the terms of financing.
Companies with plans to go public or issue bonds	Stock market regulators and institutional investors expect the internal audit charter to align with international standards (the IIA's Global Internal Audit Standards) as a reasonable precondition for a public offering or a bond issue. Adopting it early, rather than under regulatory pressure, reduces compliance costs and tactical errors in the transition.

Alignment with the pillars of good corporate governance

The Internal Audit Charter directly puts into practice the four pillars of good corporate governance:

1. Transparency. The Charter requires periodic reports of significant matters, documentation of findings and communication to the Board. Internal Audit becomes an institutional mechanism for information to flow upwards unfiltered.

2. Accountability. It sets out precisely who the Chief Internal Auditor reports to (functionally to the Audit Committee, administratively to the CEO) and how their performance is assessed. It closes the circle of control over administration.

3. Responsibility. It stipulates that the function must operate in accordance with recognised professional standards (the IIA's Global Standards, the COSO framework) and maintain a quality assurance programme that verifies compliance.

4. Fairness. By providing an independent perspective, Internal Audit safeguards in particular the interests of minority shareholders, bondholders and other stakeholders not involved in daily management.

Group Governance and Internal Audit

Where a company is part of a group, the Internal Audit function can be organised in various ways:

1. **Centralised group function:** a single Internal Audit department serves all the companies in the group. It is efficient and consistent, but requires clear rules on budgeting, priorities and reporting to various committees or to the parent company. In this case, it is important to distinguish between subsidiaries with mixed ownership (with and without controlling interest) and those the company owns outright, as the functional and reporting lines vary in each case. Generally, controlled mixed-ownership companies will require a hybrid system (see below) to prevent the parent company from gaining access to inside information through its internal audit function.
2. **Independent functions by company:** each company within the group has its own Internal Audit department, coordinated at group level. Greater independence, higher cost.

G20/OECD Principles of Corporate Governance (2023)

The G20/OECD Principles of Corporate Governance state that the Board must ensure the integrity of the company's accounting and financial systems, including an independent audit and adequate control systems.

To this end, the Principles recognise that the Internal Audit function must operate independently of management, report to the Board (typically through the Audit Committee) and have sufficient resources to fulfil its mandate.

Beyond controls: auditing corporate culture

Internal Audit is increasingly expected not only to assess processes and controls, but also to monitor organisational culture and risk culture – that is, the behaviours, decisions and attitudes that the organisation tolerates and encourages. Three key areas to consider have been identified:

- **Top-down approach:** how does the Board prioritise risk management? What is your risk appetite and how do you communicate it?
- **Day-to-day risk management:** are there regular meetings? Do managers escalate problems?
- **People management:** do incentive schemes reinforce or undermine a culture of control?

Source: IBGC and IIA Brazil.

3. **Hybrid model:** a central function defines the methodology and oversees the process, but certain local audits are carried out by teams within each company.

The choice depends on the size and independence of the companies. In all cases, the Charter must specify which companies they apply to, how findings are reported to each board, and how independence from local management is maintained.

References to international standards

The draft Charter must be brought into line with the main professional and corporate governance standards:

- Global Internal Audit Standards (2024) of the Institute of Internal Auditors (IIA). Internationally recognised standards for professional practice. They include specific requirements on the Internal Audit Charter (Standard 6.2) and Organisational Independence (Standard 7.1). View them here.
- Three Lines Model (IIA, 2020). A framework that places Internal Audit as the third line, complementary to operational management (first line) and risk and compliance functions (second line). View them here.
- COSO Internal Control Framework (2013). A framework for evaluating the internal control system, which is one of the focuses of the audit. View the executive summary here.

2. KEY COMPONENTS AND STRUCTURE

The following model provides a basic structure for drafting Internal Audit Charter. Companies are invited to adapt this model according to their specific needs. Texts in italics and with a grey background represent the suggested draft, while annotations in the margins or highlighted boxes offer practical guidance for completing each section.

[Cover Page]

INTERNAL AUDIT CHARTER

Contents:

Keep the glossary brief. Only include terms that are actually used in the Charter.

If the company is part of a group, specify the scope here: a single company, several companies or the whole group?

CHAPTER I: DEFINITIONS AND REGULATORY FRAMEWORK

1.1. *For the purposes of this Charter, the following terms shall be defined as follows:*

- *Internal Audit: an independent and objective assurance and advisory activity designed to add value and improve the operations of [Company Name] by assessing the effectiveness of risk management, internal control and corporate governance processes.*
- *Chief Internal Auditor (CIA): the person responsible for leading the Internal Audit function and reporting to the Audit Committee in accordance with this Charter.*

- *Audit Committee: a committee of the Board of Directors responsible for overseeing the Internal Audit function in accordance with its Rules of Procedure.*
- *Annual Internal Audit Plan: a work programme to execute during the financial year, drawn up on the basis of a risk assessment.*

***1.2.** The Internal Audit function must comply with the Global Internal Audit Standards of the IIA, the Code of Ethics and the applicable legislation.*

CHAPTER II: PURPOSE, MISSION AND SCOPE

***2.1. Purpose.** Internal Audit provides independent and objective assurance and consultancy services, with the aim of adding value to and improving the operations of [Company Name]. It assists the Company in achieving its objectives through a systematic and disciplined approach to assessing and improving the effectiveness of risk management, internal control and corporate governance processes.*

***2.2. Position in the control model.** The Internal Audit function constitutes the third line of defence in the Company's risk management model, complementing operational management (first line) and the risk management and compliance functions (second line). It does not replace or assume the responsibilities set out in the preceding lines.*

***2.3. Scope.** The scope of Internal Audit covers all processes, departments, systems and subsidiaries of the Company, without restriction, and includes at least:*

- *Financial audits (reliability of financial information).*
- *Operational audits (effectiveness and efficiency of operations).*
- *Compliance audits (of laws, regulations and internal policies).*
- *Information technology audits (including cybersecurity).*
- *Strategic audits and reviews of critical processes.*
- *Support in investigations of alleged fraud or irregularities.*

CHAPTER III: INDEPENDENCE, OBJECTIVITY AND AUTHORITY

***3.1. Organisational independence.** Internal Audit is independent of the departments and functions it audits. To preserve this independence:*

a) The function reports functionally to the Audit Committee and, through it, to the Board of Directors.

If an Audit Committee has not yet been established, include the definition and address the situation in the transitional provisions.

Explicit adherence to the IIA's Global Standards is the recommended practice. If the company operates in a regulated sector, include a reference to the relevant

Key concept

Clarifying the concept of the 'third line' is important: it prevents the Internal Audit function from being asked to carry out tasks that fall within the remit of management (first line) or compliance (second line).

Tailoring the Scope

If the company has subsidiaries, make it clear that they are included within the scope.

Adapt the list of audit types to the risk profile: in industry, add quality audits; in technology, add digital product audits; in agribusiness, add ESG audits.

Avoid wording that limits the scope to "the CEO's discretion" or similar: the scope is defined by the Annual Plan approved by the Committee.

b) The function operates as an independent budget centre.

c) Neither the Chief Internal Auditor nor the department staff will assume operational, executive or decision-making responsibilities in auditable areas.

d) The remuneration of the Chief Internal Auditor will not be linked to the financial performance of specific business lines or departments.

3.2. Objectivity. *Each member of the Internal Audit staff must remain impartial, avoid conflicts of interest and refrain from auditing departments in which they have had operational responsibility for a minimum period of [12 months].*

3.3. Authority. *The Internal Audit function is authorised by the Board of Directors to:*

a) Access all information, records, systems, facilities and personnel of the Company relevant to their work without restriction.

b) Allocate resources, set frequencies, select departments and apply methodologies to comply with the Annual Plan.

c) Obtain the necessary assistance from the staff of the audited departments, as well as from external professional services when specialised expertise is required.

d) Meet in private with the Audit Committee without the presence of Senior Management.

CHAPTER IV: LINES OF REPORTING AND ACCOUNTABILITY

4.1. Functional reporting. *The Chief Internal Auditor reports functionally to the Audit Committee of the Board of Directors regarding:*

a) Their appointment, performance appraisal and removal from office, all of which shall be approved by the Audit Committee and ratified by the Board.

b) Approval of this Charter and its amendments.

c) Approval of the Annual Internal Audit Plan and any significant modifications.

d) Approval of the function's budget and resources.

e) Reporting of significant findings, monitoring of corrective actions and matters that require escalation.

f) Regular interaction with the Committee, including private sessions at each meeting.

4.2. Administrative reporting. *The Chief Internal Auditor reports administratively to the [Managing Director/ CEO] exclusively*

Key concept

These four elements are non-negotiable.

- The functional reporting line to the Committee (rather than to the CEO or CFO) is the primary safeguard of independence.
- An independent budget avoids the classic pressure tactic: "If you persist with that finding, we'll cut your team's funding next year."
- It is the prohibition on carrying out operational tasks that distinguishes Internal Audit from Internal Control (which does carry out controls).
- The remuneration clause ensures that the CIA's bonus does not depend on not "upsetting" any department.

A common pitfall in family businesses

In companies where the owners are actively involved, the idea often arises that the auditor "reports directly to the owner". This may be practical, but it creates a risk: if the owner is simultaneously a shareholder, a member of the Board and an executive figure, the reporting line ceases to be independent. The recommended practice is to maintain the reporting structure to the Audit Committee (or to the full Board where no such committee yet exists), where decisions are

for the purposes of day-to-day operational coordination, including the management of human resources within the department, the implementation of the approved budget and compliance with the Company's general administrative policies.

4.3. Access to the Chair of the Committee and the Board. *The Chief Internal Auditor will have direct access to the Chair of the Audit Committee and, where appropriate, to the Chair of the Board of Directors, without the need for Senior Management to intervene.*

4.4. Mandatory communications*. The following matters shall be reported immediately to the Audit Committee, without waiting for the regular reporting cycle:*

- *Material control deficiencies.*
- *Reasonable grounds for suspecting fraud.*
- *Restrictions on the scope of work or access to information.*
- *Any undue pressure on the department or on the CIA.*

CHAPTER V: ORGANISATION AND RESOURCES

5.1. Operating model. *The Internal Audit function will be carried out under the following model: [in-house / hybrid (co-sourced) / outsourced]. The decision on the model will be reviewed by the Audit Committee at least every [3 years] or when justified by significant changes in the risk profile.*

5.2. Structure. *The function will be led by the Chief Internal Auditor and will have sufficient staff, own or hired, to execute the approved Annual Plan.*

5.3. Resources. *The Company will provide the function with the financial, human and technological resources necessary to fulfil its mandate. The annual budget and resource plan will be proposed by the Chief Internal Auditor and approved by the Audit Committee.*

5.4. Resource limitations. *If, at any time, the Chief Internal Auditor considers that the resources allocated are insufficient to comply with the Annual Plan or this Charter, they must formally notify the Audit Committee, indicating the impact on assurance coverage.*

5.5. Competencies. *The Internal Audit team as a whole must possess knowledge of accounting and financial reporting, internal control (the COSO framework), risk management, information technology and the Company's industry. Where the complexity of a task exceeds the organisation's in-house capabilities, specialist professional services may be contracted.*

5.6. Training. *The department will maintain an annual training programme to ensure that staff receive ongoing professional development.*

Key concept

Medium-sized companies are usually better served by hybrid models (co-sourced): an in-house CIA coordinates the work, while an external firm provides expertise (IT, fraud, etc.).

Full outsourcing may be appropriate for small companies with limited risks, but care must be taken to ensure the supplier's independence (it must not be the same firm as the external auditor).

Competencies are assessed as a whole, not individually. A small team can be effective if it brings together a diverse range of skills or supplements its

CHAPTER VI: RESPONSIBILITIES OF THE Chief Internal Auditor

6.1. *The Chief Internal Auditor has the following personal and non-transferable responsibilities:*

a) To develop and propose the Annual Internal Audit Plan based on a documented risk assessment.

b) To implement the approved Annual Plan and report its progress to the Audit Committee.

c) To issue audit reports and communicate significant findings.

d) To immediately escalate matters affecting financial integrity, material internal controls, or ethical conduct.

e) To maintain a programme to ensure and improve the quality of the function.

f) To coordinate with external audit and second line functions to optimise coverage without impacting independence.

g) To attend Audit Committee meetings as a non-voting participant when requested, including closed-door sessions.

h) To keep the Committee informed of emerging trends, regulatory changes and best practices in Internal Audit.

i) To advise the Audit Committee on the scope of the external auditor's work and support its evaluation.

j) To support investigations of alleged fraud and report results to the Audit Committee.

k) To ensure the professional development and training of departmental personnel.

CHAPTER VII: ANNUAL INTERNAL AUDIT PLAN

7.1. Risk-based methodology. *The Annual Plan will be drawn up using a risk-based approach, through a documented assessment that takes into account the Company's strategies, objectives and risks. The assessment will be conducted at least annually.*

7.2. Contributions. *The Chief Internal Auditor will consider the contributions of the Board of Directors, Senior Management, and the risk management and compliance functions. The Chief Internal Auditor has the final say in drawing up the Plan, subject to approval by the Audit Committee.*

7.3. Approval. *The Annual Plan will be submitted to the Audit Committee for review and approval, along with the schedule, required resources and associated budget.*

7.4 Modifications. *The Plan may be modified during the year. Significant modifications — those that alter scope, risk prioritisation or coverage — will require prior approval from the Committee.*

Terms of Reference (ToR) — the supplement to the Charter

The Charter sets out the institutional framework for the function. The Terms of Reference (ToR) break this framework down into specific job profiles. Two sets of ToR are usually prepared:

- **ToR of the Chief Internal Auditor:** job profile, specific responsibilities, minimum training and experience, certifications (CIA, CPA, CISA), technical and behavioural competencies, and evaluation criteria. They are used for hiring processes and for annual performance evaluation.
- **General ToR of the Internal Audit function for each team member**.

ToR are essential tools for ensuring that the Charter is translated into specific practices. It is good practice to include them as annexes to the Charter or as separate documents to which explicit reference is made (see Annex I).

Key concept

'Risk-based' means that the Plan is not a mechanical rotation of areas, but rather an allocation of resources proportional to the materiality of the risks.

It is good practice to document the risk assessment: if, in the future, questions arise as to why X was audited and not Y, the document will provide the answer.

Operational modifications will be documented and reported in the periodic reports.

7.5. Minimum coverage. *Without prejudice to the risk-based approach, the Plan must ensure periodic coverage of:*

- *The financial reporting process.*
- *Controls over significant assets.*
- *Critical compliance processes.*
- *The risks of information technology and cybersecurity.*
- *Fraud-related risks.*

CHAPTER VIII: AUDIT PROCESS AND RESULTS REPORTING

8.1. Execution. *Each audit engagement will be planned on a case-by-case basis, with clearly defined objectives, scope, criteria and procedures. Working papers and evidence must be documented in accordance with the methodologies of the function.*

8.2 Audit reports. *At the end of each engagement, a written report will be issued including at least:*

a) Background and objectives.

b) Scope and procedures applied.

c) Findings, with criteria, condition, cause, effect and recommendation.

d) Response from the management of the audited department and agreed action plan, specifying those responsible and the deadlines.

e) Overall conclusion of the engagement.

8.3. Distribution of reports. *The reports will be distributed to the management of the audited department and to the Chief Executive. The summary and significant findings must be reported to the Audit Committee in accordance with section 8.5.*

8.4. Follow-up. *The function will maintain an open record of findings and recommendations, with documented monitoring of progress until they are effectively implemented. The status of the record will be reported to the Committee on a regular basis.*

8.5. Reports to the Audit Committee. *The Chief Internal Auditor shall submit to the Committee, at least on a quarterly basis:*

a) Progress of the Annual Plan.

b) Summary of significant findings from the period.

c) Status of the recommendations tracking log.

d) Emerging issues and observations regarding the control environment.

Key concept

The audit process is not a unilateral act. When the Internal Audit department issues recommendations, the management being audited must comment on them. The auditor will review the comments and decide whether to amend or uphold them. Management will then draw up an action plan, and the auditor will assess the effectiveness of the plan. That is when the report will be submitted to the Committee through the CIA. If management disagrees, that disagreement is documented and also escalated; it is not concealed.

The structure of the report (criterion – condition – cause – effect – recommendation) is standard practice and facilitates subsequent follow-up.

The administration's response must be included in the report: it is not a concession; it is what makes the audit a tool for improvement, rather than merely a means of reporting wrongdoing.

It is good practice for each audit to produce two outputs:

- **Executive summary (short):** for the Audit Committee and the Board: critical issues, significant findings, conclusions.
- **Detailed (long) report:** for the audited management and for the records: scope, procedures, evidence, detailed recommendations, agreed action plan.

8.6. Immediate escalation. *Significant matters — material misstatements, indications of fraud, governance failures — will be escalated to the Audit Committee immediately, without waiting for the regular cycle.*

CHAPTER IX: COORDINATION WITH THE EXTERNAL AUDITOR AND OTHER FUNCTIONS

9.1. Coordination with external audit*. The function will maintain a professional working relationship with the Company's external auditor, with the aim of:*

a) Ensuring adequate audit coverage and avoiding duplication of effort.

b) Sharing relevant information about risks, findings and areas of common interest.

c) Supporting the Audit Committee in assessing the independence, quality and performance of the external auditor.

This coordination will not affect the independence of either function.

9.2. Coordination with the second line. *The function will liaise with the risk management, compliance, quality and other functions that make up the second line of defence, in particular to:*

a) Exchange risk assessments and records of findings.

b) Align working plans for adequate coverage.

c) Validate information and controls associated with risk indicators.

This coordination should not entail the subordination or delegation of the Internal Audit department's independent assurance responsibilities.

9.3. Relationship with the Integrity Committee or equivalent body. *Where the Company has [an Integrity Committee or a Compliance Officer], the Internal Audit department will report relevant findings within its remit to them and coordinate the follow-up of corresponding corrective measures.*

CHAPTER X: QUALITY ASSURANCE AND CONTINUOUS IMPROVEMENT

10.1. Quality assurance and improvement program. *The Chief Internal Auditor will develop and maintain a quality assurance and improvement programme that assesses compliance with the Global Standards for Internal Auditing, this Charter and the defined performance objectives.*

10.2. Internal evaluations. *It will include:*

- *Ongoing quality control of audit engagements, including the review of working papers.*

Key concept

External audits and internal audits are not substitutes for one another. The external audit comments on the financial statements; the internal audit assesses the entire control system.

Sharing information with the external auditor is good practice, but the CIA cannot become the external auditor's 'assistant'; they must maintain

Technology in the Internal Audit function

The use of data analytics, continuous monitoring and, progressively, artificial intelligence tools is transforming practice. According to the global survey "Internal Audit: Vision 2035" (Internal Audit Foundation, 2024), 91% of audit leaders consider data analysis to be extremely or very important for the future of the profession. Medium-sized companies don't require sophisticated infrastructure: an initial basic analysis of transactional data (purchases, payments, sales) already generates value.

- *Regular self-assessments of the function's compliance with the Standards, its methodologies and performance targets.*

10.3. External evaluations. *At least every [five (5) years], the function should be subject to an external quality assessment carried out by a qualified independent assessor who is not affiliated with the Company or the business group to which it belongs.*

10.4. Communication of results. *The results of internal and external assessments, as well as the action plans to address opportunities for improvement, should be reported to the Audit Committee and the Board of Directors.*

10.5. Performance indicators. *The function will maintain key indicators to measure its effectiveness, which will include at least the following: compliance with the Annual Plan, timeliness of reports, rate of implementation of recommendations, stakeholder satisfaction and staff training hours.*

Key concept

Small businesses can ensure compliance by carrying out simple self-assessments and cross-checks; no complex infrastructure is required.

The IIA standard is an external evaluation every 5 years. For small businesses, a "self-assessment with independent validation" is an accepted alternative.

The external evaluator must NOT be the Company's external auditor or a company with a material relationship.

CHAPTER XI: VALIDITY, REVIEW AND APPROVAL

11.1. Approval and validity. *This Charter shall come into force upon their approval by the Board of Directors, following a recommendation from the Audit Committee, and shall supersede any previous version.*

11.2. Periodic review. *The Charter shall be reviewed at least once a year by the Audit Committee and, where appropriate, amended to reflect:*

a) Significant changes in the structure, strategy or risks of the Company.

b) Amendments to the applicable Professional Standards.

c) Regulatory changes affecting the function.

d) Lessons learned in the operation of the function.

11.3 Amendments. *Amendments to the Charter shall be proposed by the Chief Internal Auditor, recommended by the Audit Committee and approved by the Board of Directors.*

11.4. Version control. *A version control log shall be maintained, documenting the date of each revision, the approval dates, the changes made and the current version.*

11.5. Disclosure. *The Charter will be communicated to Senior Management and the relevant staff, and will be referred to in the Company's annual corporate governance report. [Once the Company is listed on the stock exchange, the Charter will be available on the corporate website].*

Transitional provisions (where an Audit Committee has not yet been established)

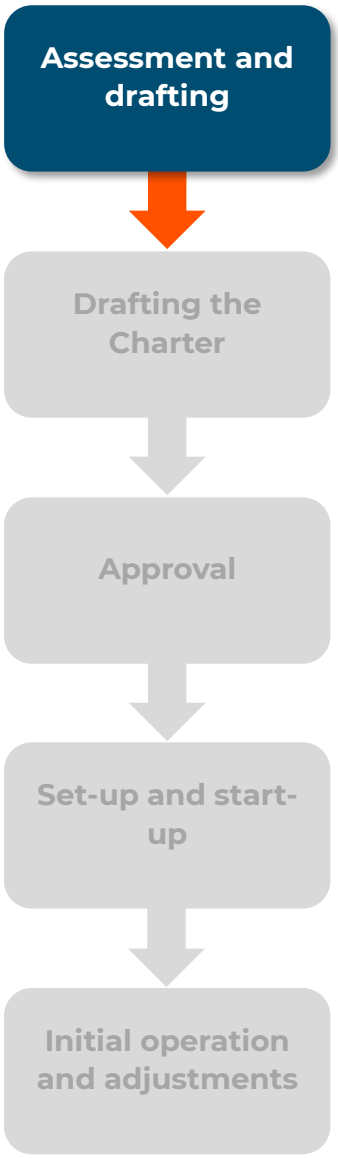
12.1. Transitional period. While the Company does not have a formally constituted Audit Committee ("Transitional Period"), the functions, powers and responsibilities assigned to the Audit Committee by this Charter shall be exercised by the Board of Directors as a whole.

12.2. No individual delegation. During the Transitional Period, the Committee's powers shall not be deemed to have been delegated to the Chair of the Board or to any individual Board member. Decisions must be made collectively.

12.3. Incorporation period. The Company sets a target deadline of [___] months from the date of approval of this Charter for the formal establishment of the Audit Committee.

3. STEP-BY-STEP IMPLEMENTATION GUIDE

Adopting a Charter is the beginning, not the end. Effective implementation of the Internal Audit function requires an orderly process that typically takes between 12 and 16 weeks in medium-sized companies.



Assessment and drafting phase

1

3-4 weeks

The starting point is to understand what is currently in place. Skipping this stage is the most common reason why Charters end up as mere desk-bound documents, with no real impact.

Key activities

- *Mapping of the current situation.* Identify if there is a control function known as "Internal Audit" or similar, who it reports to, what it does, what resources it has, and how it is perceived by the Board and management.
- *Preliminary risk analysis.* An initial assessment of the company's risk profile: sector, size, operational complexity, regulatory exposure, critical technology platforms. It will be used to determine the scale of the operational model.
- *Definition of the operating model.* Key decision: in-house, co-sourced or outsourced. This decision should be taken by the Audit Committee (or the Board, if no such committee exists) on the basis of cost, the level of expertise required and the availability of local talent.
- *Resource estimating.* Number of people, estimated annual budget, necessary technological tools. Without a preliminary assessment, the Charter may approve mandates that are impossible to fulfil.
- *Survey conducted by an external auditor.* A discussion with the company's external auditor helps to identify critical areas that are already under external scrutiny and to understand mutual expectations.

Deliverable

A document covering initial assessment and drafting, containing: the current situation, a preliminary risk map, the recommended operational model, an estimate of resources and a timetable for the subsequent phases.

Charter drafting phase

2

3 weeks

The assessment will facilitate drafting the Charter: the text reflects decisions that have already been taken.

Key activities

- *Adaptation of the template.* Take the template from Chapter 2 of this guide and adapt it to the company's specific circumstances (names, scope, operating model, deadlines). Resist the temptation to copy word for word: every company is different.
- *Validation with key areas.* Share the draft with the CEO, CFO, legal department and external auditor before presenting it to the Committee. This validation minimises surprises during the approval process.
- *Iterations.* Wait for two or three rounds of feedback. This is normal and desirable: each iteration refines the document.
- *Preparation of the ToR.* At the same time, draft the general Terms of Reference and those for the CIA. Although they are not formally part of the Charter, they are essential for the next stage.

Deliverable

Draft Charter, validated with key areas, ready to be submitted to the Audit Committee (or the Board). Accompanied by draft ToR (see Annex I).

Approval phase

3

2 weeks

Approval is a formal act, but it also serves an educational purpose as it allows the Board to understand what it is approving and what it is committing to uphold.

Key activities

- *Review by the Audit Committee.* The Committee will review the draft, make comments and issue its recommendation to the Board. In companies without a Committee, this step is carried out directly by the Board in a specific session.
- *Adoption by Board.* The Board of Directors approves the Charter as a formal act recorded in the minutes. This procedure

must be carried out precisely: approval of the full text, date of entry into force, and instructions for internal publication.

- *Communication to the organisation.* Once approved, senior management and the relevant staff should be informed. The function cannot operate if the organisation does not know that it exists or what authority it has.
- *Archiving and version control.* To establish the formal repository for the Charter (corporate governance folder, with version control).

Deliverable

Charter approved by the Board, communicated to the organisation and formally filed with a version number.

Set-up and start-up phase

4

4-5 weeks

The CIA is hired or appointed, the first Annual Plan is prepared, and the first audit is carried out.

Key activities

- *Hiring and appointment of the CIA.* If the role doesn't already exist, this is the time to recruit. The hiring process must respect the role of the Committee: although HR may carry out the process, the final decision rests with the Committee (or the Board during the transitional period).
- *Induction and onboarding.* The CIA should meet the members of the Board, Senior Management, external auditors and those responsible for the second line. This stage of relationship-building is crucial to future effectiveness.
- *First risk analysis.* The CIA carries out its own risk assessment, now with full access to information. This assessment is the basis of the first Annual Plan.
- *First Annual Plan.* Draft a prudent Annual Plan: 4-6 audit tasks in the first year, enough to build credibility without overburdening the organisation or the team.
- *Approval of the Plan by the Committee.* The Committee approves the Annual Plan and associated budget. From here, the function is operational.

Deliverable

CIA appointed and working. First Annual Plan approved. First audit cycle started.

Quick Wins

The first two or three audits should focus on areas where quick, visible results can be achieved, to build credibility. Avoid tackling politically contentious issues in the first year.

Initial operation phase and adjustments 5

Continuous, first 6 months

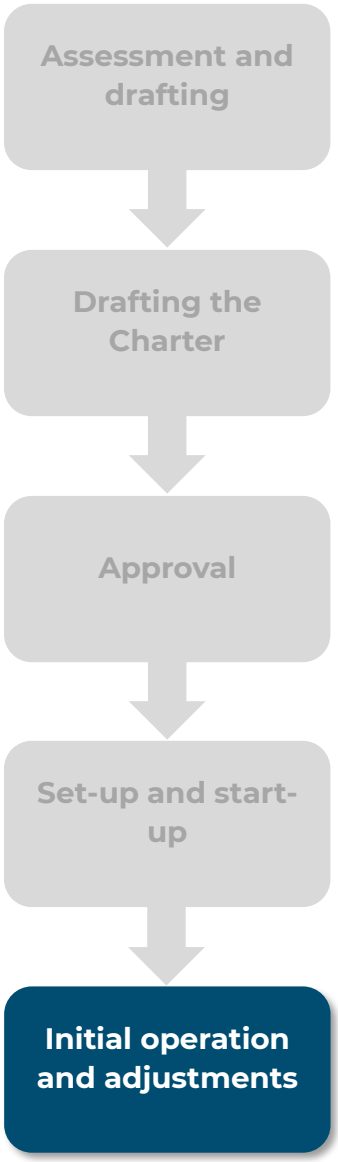
The first six months shape the long-term culture of the department. It is the time to fine-tune methodology, the level of detail in reports, the frequency of communications and relationships with the various departments.

Key activities

- *Execution of the first audits.* Apply methodology, document working papers and issue reports with responses from management.
- *First quarterly report to the Committee.* A concise yet comprehensive executive report setting out the Plan's progress, key findings and the status of recommendations.
- *Private meeting with the Committee.* At the Committee's first meeting with the CIA, establish the practice of holding the session in private (without management present). It is easier to establish the practice from the beginning than to introduce it later.
- *Adjustments to methodology.* Following the initial audits, review and amend templates, criteria for classifying findings, and report formats.
- *Quality Assurance Programme.* Set out how internal monitoring will be carried out and when the first external evaluation will take place (typically in year 5).
- *First evaluation of the function.* At the close of the first annual cycle, an honest assessment: was the Charter complied with? What needs to be adjusted?

Deliverable

Function operating effectively; first quarterly reports been submitted; first assessment of compliance with the Charter carried out; and proposals for improvement identified for the next review.



4. TIME CONSIDERATIONS

When to address the Internal Audit Charter is as important a question as how to draft them. There are times when the cost-benefit changes dramatically.

Triggers that the Charter recommends addressing

Generational succession. In family businesses, generational succession is a natural opportunity to improve the professional standards of the control functions and formalise processes that previously relied on personal trust.

Adverse events. Detection of fraud, material errors in financial statements, regulatory sanctions, shareholder claims. Although these are not the ideal trigger, they are usually the most persuasive. In such cases, the Charter is usually adopted alongside a comprehensive remediation process.

Growth in size and complexity. When a company exceeds the thresholds beyond which the CEO's or founder's informal control ceases to be effective, typically when a certain number of employees, regions or business lines are reached.

Entry of institutional investors. Investment funds, multilateral banks such as IDB Invest, and development institutions often require or expect such a charter to be in place as a condition of investment or as a milestone in their corporate governance strengthening programme.

Public offering or bond issuance processes. Before going public, the company must demonstrate that it has a sound corporate governance framework. Doing so under regulatory pressure is more expensive than doing it in advance.

Recommendation of the external auditor or consultant. When an external adviser identifies material weaknesses or areas for improvement in the internal control system.

Review and update cycle

The Charter must be active, not left on the shelf. Best practices include:

- **Mandatory annual review.** Once a year, the Audit Committee reviews the Charter and verifies whether they require updating. If there no changes are required, the revision is documented without modifications.
- **Review by event.** When a significant change occurs within the company (merger, acquisition, change in business model, regulatory changes) or in professional standards, the Charter should be reviewed outside the regular cycle.

- **Review following external evaluation.** The external quality review (carried out every five years) usually identifies areas of improvement for the Charter. Their recommendations trigger an ad hoc review.

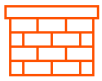
Integration with the annual corporate governance calendar

The Internal Audit Charter does not operate in isolation from other governance instruments. Integration with the annual calendar is key to avoiding duplication and capitalising on synergies:

- **Q1:** Approval of the Annual Internal Audit Plan by the Committee. The CIA presents their risk assessment.
- **Q2-Q3:** Plan execution. Quarterly reports to the Committee on progress, significant findings and status of recommendations.
- **Q4:** Review of the Charter by the Committee. Assessment of CIA performance. Preparation of the Annual Plan for the following year. Annual report on the activities of the function.
- **Annually:** Communication to the Board in full compliance with the Charter. Inclusion of relevant information in the annual corporate governance report.

5. IMPLEMENTATION CHALLENGES AND CRITICAL SCENARIOS

Typical implementation challenges



Internal resistance to the function. The introduction of a formalised internal audit function can cause unease among management teams accustomed to operating without systematic scrutiny. The most common examples include: delays in providing information, the auditor being informally described as "unfamiliar with the business", pressure to diminish findings, attempts to influence the scope of audits.

Recommended answer: The Charter is the main tool. When resistance arises, the answer is not to negotiate; it is to take the matter to the Committee. The existence of the possibility of escalation, rather than its use, is usually sufficient to reorder behaviour.

Confusion between Internal Audit and other control functions. There can often be confusion during the first few months about what falls within the remit of Internal Audit and what falls within the remit of other departments (Compliance, Risk, Operational Internal Control). This confusion can lead to duplication, gaps and conflicts.

Recommended response: apply the Three-Line Model. Management operates and designs controls (first line); which are monitored by risk and compliance (second line); while internal audit assesses the effectiveness of the entire system (third line). The Charter must make this distinction explicit.

Insufficient resources. A situation so common that it is practically the norm: the appointed CIA discovers that the approved budget is insufficient to fulfil the Plan, or that the team is too small to provide the coverage that has been committed to.

Multidisciplinary teams and guest auditors

Given the pace of change in the business environment, Internal Audit teams should draw on a diverse range of backgrounds (accounting, IT, engineering, ESG, law). When a specific audit requires expertise that the team does not possess, a useful approach is to bring in a "guest auditor": a specialist professional, either hired on an ad hoc basis or seconded from another department, who joins the team under the leadership of the CIA solely for that assignment. It is particularly useful for medium-sized companies with limited budgets.

Recommended response: formally document the inadequacy to the Committee, explicitly identifying which areas may not be covered. The function cannot assume assurance risks due to lack of resources: if there are no resources, some areas are not covered. Transparency is the right approach.

Findings affecting Senior Management. Sooner or later, an audit will uncover findings that implicate a member of Senior Management. It is the most sensitive and, at the same time, the most defining aspect of the culture of the function.

Recommended response: apply the rules of communication and escalation provided for in the Charter. Private meetings with the Committee are the channel specifically intended for such cases. The CIA does not make disciplinary decisions; it reports findings and allows the Committee and Board to decide.

"What-If" Scenarios

“What if the CEO or Senior Management restricts access to information?”

This is a direct violation of the Charter. The response must be proportionate but firm: first, a formal written request setting out the restriction and its impact; if the issue persists, it must be referred to the Committee. A restriction on scope is one of the matters that must be reported to the Committee immediately, in accordance with section 4.4 of the model Charter.

“What if an audit cannot be completed due to lack of resources during the financial year?”

Document the situation, assess options (prioritisation, postponement, engaging external support) and inform the Committee before implementing the solution. Do not cancel audits under the Plan without the Committee’s approval; any material changes require prior approval.

“What if the findings are not addressed by management?”

This is an especially worrying pattern because it implies that the assurance cycle does not close. The CIA must maintain an open register of recommendations, escalate overdue recommendations to the Committee and, in cases of systematic non-compliance, recommend that the Committee take specific action (interviews

When to escalate to the full Board (not just the Committee)

There are exceptional circumstances in which the CIA must refer the matter to the full Board and not just to the Audit Committee:

- Evidence of misconduct involving one or more members of the Committee.
- Serious restrictions on scope that the Committee fails to resolve within a reasonable timeframe.
- Conflicts of interest on the part of the Committee in relation to the matter reported.

In such cases, the CIA carefully documents the reasons for referring the matter to the full Board, preserves the evidence and notifies the Chair of the Board. It is an extreme situation, but the Charter must allow it.

with those responsible, reassignment of responsibility, review of the performance appraisal of the person responsible).

“What if the external auditor and the CIA have different views on a matter?”

Let's imagine a very possible scenario. The external auditor expresses an opinion on the financial statements; the CIA takes a broader view. If the differences are material, both should present their positions to the Committee, which will decide whether it requires further analysis. The Charter doesn't exist to hide disagreements: making them visible to the Committee is part of the role of the Internal Audit function.

“What happens if the organisation reappoints the CIA too quickly?”

Frequent reappointment of the CIA is a cause for concern regarding the true independence of the institution. The Charter stipulates that the Committee must approve the appointment and dismissal of the CIA; the Committee must document the reasons and, if it detects a pattern, report this to the full Board or consult with the Chair of the Council. It is good practice for the CIA to be given the opportunity to address the Committee prior to any dismissal, so they can present their case.

6. ANNEXES AND RESOURCES

Glossary of Terms

Below, we present a comprehensive glossary of terms used in this document, including the terminological variations across major Latin American and Caribbean countries.

Term used	Definition
Assurance	An objective assessment covering processes, controls, risks and governance, designed to provide the Board and senior management with an independent opinion on their effectiveness.
External Audit	Audit carried out by an external firm, mainly on the financial statements. It is independent of the organisation and issues a public professional opinion. Distinct from Internal Audit.
Internal Audit	An independent organisational function that assesses governance, risk management and internal control processes. Reports to the Audit Committee/Board.
Internal Audit Charter/Statute/Regulations	Various names for the document that formalises the Internal Audit function. "Charter" is the English term; "Estatuto" [Statute] is common in countries such as Mexico, Argentina and Chile; "Reglamento" [Regulations] is common in countries such as Colombia, Peru and Central America. They refer to the same document.
Audit Committee	A committee of the Board of Directors (known as the Consejo de Administración, Junta Directiva, Directorio or Consejo de Administración in Spanish-speaking countries) responsible for overseeing internal and external audits.
Board of Directors	A collegiate body elected by the shareholders to oversee the management of the company. Also known as the Junta Directiva (Colombia, Venezuela), Directorio (Chile, Peru, Argentina, Uruguay), or Consejo (Mexico, Spain).
Auditors / Trustees	In some countries, a term used to refer to oversight bodies that complement the Board or the Internal Audit function. They are not substitutes for Internal Audit.
Finding	A specific conclusion from an audit that identifies a discrepancy between the observed condition and the applicable criteria. It usually includes a cause, effect and recommendation.
Chief Internal Auditor (CIA)	The person in charge of the function. Also known as the Chief Audit Executive (CAE).
Terms of Reference (ToR)	An operational document that describes the role, responsibilities, and profile of a post or function. It supplements the Charter.

Annex I: Terms of Reference (ToR) of the Chief Internal Auditor

The Terms of Reference describe the role profile, its specific responsibilities, and the criteria for hiring and evaluation. They are a complement to the Charter, not a substitute for them. This is a simplified version. The following template should be reviewed with local legal advice before use.

[Company Name]

1. Identification of the role

Title: Chief Internal Auditor (CIA)

Functional report: Audit Committee of the Board of Directors

Administrative report: [Managing Director/CEO]

Type of contractual relationship: [Company Employee/Independent Professional/Contracted Firm]

Status: [Full-time/Part-time /Professional Services]

Place of work: Headquarters of the Company, with availability to visit branches and subsidiaries.

2. Job purpose

To lead the Internal Audit function in accordance with the Charter approved by the Board, ensuring the provision of independent and objective assurance services regarding the Company's corporate governance, risk management and internal control processes.

3. Main responsibilities

- **Function leadership.** To lead the Internal Audit function in accordance with the Charter, maintaining independence and objectivity.
- **Risk assessment and planning.** To conduct the Organisation's risk assessment annually and present the Annual Internal Audit Plan to the Audit Committee.
- **Execution of the Plan.** To ensure the timely execution of the Plan, managing own resources and, where appropriate, hiring specialised professional services.
- **Communicating with the Committee** To report quarterly to the Committee, attend its meetings, hold private sessions and immediately escalate significant matters.
- **Management of findings.** To maintain the open record of findings and recommendations, monitor their implementation, and report their status to the Committee.
- **Coordination.** To coordinate with the external auditor, the functions of the second line and the compliance area, without affecting independence.
- **Quality assurance.** To maintain a programme for quality assurance and improvement of the function in accordance with the IIA's Global Standards.
- **Team development.** When applicable, to lead the professional development of the team, their training and evaluation.

- **Advising the Board.** To advise the Committee and the Board on trends in risk management, internal control, corporate governance and internal audit best practices.

4. Professional profile required

Education

- *Essential:* University degree in Public Accounting, Business Administration, Industrial Engineering, Economics, Finance, or related discipline.
- *Desirable:* Postgraduate studies in auditing, finance, risk management or corporate governance.

Professional qualifications

- *Desirable (at least one):* CIA (Certified Internal Auditor), CPA/CPC (Certified Public Accountant), CISA (Certified Information Systems Auditor), CFE (Certified Fraud Examiner), CRMA (Certification in Risk Management Assurance).

Professional experience

- *Minimum:* [5-7] years in internal auditing, external auditing, risk management, compliance or related functions.
- *Desirable:* Experience in companies in the Company's sector or industry, in companies comparable in size, or in external audit firms with a recognised track record.
- *Leadership:* Previous experience leading teams or projects.

5. Technical and soft skills

Technical skills

- In-depth knowledge of the IIA's Global Internal Auditing Standards and the Three-Line Model.
- Mastery of internal control (COSO) and risk management (ERM) frameworks.
- Knowledge of accounting (IFRS/IFRS) and financial standards.
- Familiarity with IT systems, cybersecurity and data auditing.
- Knowledge of the regulatory framework applicable to the Company's industry.
- Soft skills
- Impeccable professional integrity. This is essential above all else.
- Independence of judgement. Ability to defend technical positions in the face of organisational pressure.
- Communication. Ability to communicate complex findings clearly, verbally and in writing, to technical and non-technical audiences.
- Analytical thinking. Ability to break down complex problems and identify root causes.
- Intellectual curiosity. A constant commitment to understanding the business and its processes before assessing them.
- Discretion. Careful handling of sensitive and confidential information.

6. Incompatibilities and conflicts of interest

The CIA must not be in any of the following situations, including during the [cooling-off period prior/12 months prior] to stepping into the position:

- Have held executive or operational positions in the Company or its subsidiaries.
- Have material business relationships with the Company.
- Being related by blood or marriage up to the second degree to members of the Board, senior management or controlling shareholders.
- Being disqualified due to professional or regulatory sanctions.

7. Hiring process.

- *Job posting*. The process is coordinated by the Human Resources department under the supervision of the Audit Committee (or the full Board when no such Committee exists).
- *Candidate evaluation*. Comparison of profiles against ToR, technical interviews, background checks and professional references.
- *Committee interview*. The shortlisted candidates are interviewed by the Committee, which may invite the CEO to attend, although this does not replace the Committee's decision.
- *Decision*. The Committee recommends the selected candidate to the Board of Directors. The Board has the final say.
- *Onboarding*. Once appointed, the CIA goes through an induction process that includes meeting the Board, Senior Management, external auditors and those responsible for the second line.

8. Performance evaluation

The performance of the CIA is evaluated annually by the Audit Committee, based on:

- Compliance with the Annual Internal Audit Plan.
- Technical quality of reports and findings.
- Timeliness and effectiveness of communications to the Committee.
- Rate of implementation of recommendations.
- Results of the quality assurance program.
- Contributions to the improvement of the Company's corporate governance.
- Own professional development and, where applicable, that of the team.

The remuneration of the CIA will not be linked to the financial performance of business lines or auditable departments. Any variable components will be based on indicators specific to the function.

9. Dismissal

Dismissal of the CIA must be approved by the Audit Committee and confirmed by the Board. Prior to any dismissal decision, the CIA will have the opportunity to make their case to the Committee. The reasons for the dismissal will be documented in the corresponding minutes.

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