Chartered Institute of Internal Auditors

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Andrea Tweedie
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Submitted via email to: stewardshipcode@frc.org.uk

Dear Andrea,

The Chartered Institute of Internal Auditors' Response to the UK Stewardship Code Consultation

The Chartered Institute of Internal Auditors welcomes the opportunity to respond to the Financial Reporting Council's (FRC) consultation on the revised UK Stewardship Code. Our response has been informed by extensive consultation with our members and stakeholders, including a virtual roundtable discussion with senior internal audit executives from Code signatory firms, who share the concerns outlined below.

Our main concerns regarding the Code revisions are as follows:

Revised Definition of Stewardship

The removal of explicit references to the benefits of good stewardship to the economy, environment, and society weakens the definition of stewardship and makes it less reflective of its broader purpose in today's investment landscape. In particular, investors face increasing investment risks related to climate change and societal impacts, and the revised definition does not adequately reflect these realities. The current Code definition appropriately acknowledges that responsible stewardship should deliver value for investors and lead to benefits for the wider economy, the environment and society, so the FRC should retain the existing definition.

Removal of References to Internal and External Assurance

We do not support the removal of explicit references to internal and external assurance, as these mechanisms help to ensure independent oversight and help firms demonstrate the effectiveness of their stewardship policies, processes, and activities. The 2020 Code rightly recognised assurance as a key mechanism for maintaining trust—including the role of internal audit in assessing stewardship processes. The revised Code should retain the requirement for Code signatories to explain what internal and external assurance they have received in relation to stewardship, to promote and encourage strong governance practices.

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Removal of the Escalation Principle

Escalation has always played an important role in stewardship, ensuring that signatories take action where appropriate. The removal of Principle 11 as a stand-alone principal risks reducing the prominence and importance of escalation. Without a clear and focused principle and reporting requirements, firms risk deprioritising escalation or interpreting it inconsistently, leading to a weaker Code. We urge the FRC to retain a dedicated principle on escalation to reinforce investor accountability and meaningful engagement.

These concerns, informed by engagement with our members, are discussed in greater detail in our full response below to the specific consultation questions.

We appreciate the opportunity to contribute to this consultation. The Chartered IIA is happy to discuss any comments in the response.

We are happy for our response to be published.

Yours sincerely,

Gavin Hayes

Gavin Hayes
Head of Policy and Public Affairs (and member of the FRC Stakeholder Insights Group)

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The Chartered Institute of Internal Auditors' Response to the UK Stewardship Code Consultation

Q1. Do you support the revised definition of stewardship?

The Chartered Institute of Internal Auditors (Chartered IIA) does not support the revised definition of stewardship and strongly advocates for retaining the existing definition. The removal of explicit references to the sustainable benefits of good stewardship to the economy, environment, and society is of great concern, as it risks narrowing the scope of stewardship and diminishing its role in addressing key investment risks and contributing to economic growth. The current definition remains fit for purpose, is widely supported by the stakeholders we have spoken to along with senior internal audit executives from Code signatory firms and is aligned with modern stewardship expectations. Changing it weakens confidence in the Stewardship Code's purpose and effectiveness by removing clear ESG considerations, which creates ambiguity for signatories and investors.

The Chartered IIA acknowledges the Financial Reporting Council's (FRC) intent to revise the definition of 'Stewardship' in the Code, but the proposed changes risk creating confusion rather than improving clarity. The revised definition states *"the responsible allocation, management, and oversight of capital to create long-term sustainable value for clients and beneficiaries,"* this could be interpreted as emphasising financial value creation over other important aspects of stewardship. However, removing explicit references to the benefits of good stewardship to the economy, environment, and society weakens the definition and makes it less reflective of the broader need for responsible investments in today's landscape. Senior internal audit executives from the Code signatory firms that we spoke to also felt that the proposed revised definition was too vague on what is meant by "long-term sustainable value" whereas the existing definition provides greater clarity on exactly what is meant by this. This concern was echoed in our roundtable discussion with senior internal audit executives from Code signatory firms, where participants emphasised that the proposed revision creates confusion rather than clarity. One Chief Audit Executive from a major asset management firm noted: *"The new definition could be seen as narrow, but I actually think it's broad and vague. What does 'long-term sustainable value' actually mean? It could mean different things to different stakeholders, shareholders, and clients. The existing definition provides greater clarity."*

Investors are already facing increasing material risk exposures related to environmental and social issues, including the risks associated with climate change, biodiversity loss, and modern slavery, including a significant rise in the number of greenwashing scandals involving major asset managers and the companies they invest in. Greenwashing scandals can significantly impact the financial health of the companies involved, damage their reputation, and harm their growth prospects. These effects can, in turn, negatively impact the wider economy and wealth creation. The absence of references to the sustainable benefits of good stewardship to the environment and society in the revised definition could risk making the Code misaligned with the evolving priorities of clients, beneficiaries, investors and regulatory developments, especially with the growing evidence that ESG factors contribute to long-term value creation. A Chief Audit Executive from a Code signatory firm further warned: *"We're getting a mixed message from regulators. ESG is important, then it's not. There's a high bar, but then it's removed from the Codes. And the minute something isn't explicitly referenced, that's when the thin end of the wedge starts to come in"*

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The rapid rise of ESG-related risks, particularly in relation to climate change and environmental sustainability, has been reflected in our annual Risk in Focus [1]research which is based on a survey of 985 Chief Audit Executives across Europe. Last year's survey found that one-third of the Chief Audit Executives identified climate change, biodiversity, and environmental sustainability as a top five risk, and this is forecast to rise to 50% by 2028. This sentiment is also increasingly reflected by leaders across the investment community with climate and ESG risks being recognised as investment risks.

The 2020 Code definition appropriately acknowledged that responsible stewardship delivers sustainable value not only for investors but also leads to benefits for the economy, the environment, and society. The current definition helps to reinforce the point that a focus on ESG factors can significantly support higher levels of economic growth and investment. There is evidence that integrating ESG into business strategies can lead to sustainable growth with studies showing a positive correlation between ESG practices and financial returns in the majority of cases[2]. Furthermore, a study by McKinsey found that around 85% of Chief Investment Officers now consider ESG factors key to their investment decisions, with around 80% evaluating how ESG impacts projected cash flows for the companies they were looking to invest in[3]. The Chartered IIA therefore disagrees with the suggestion that the inclusion of "leading to benefits" in the 2020 definition implied the prioritisation of societal and environmental benefits over financial returns. Instead, this language rightly recognised the increasingly interconnected nature of financial, economic, societal, and environmental outcomes. Removing these references risks narrowing the scope of stewardship and creating a perception that the Code no longer fully aligns with the complexities and risks associated with modern investment strategies. This move is concerning in an increasingly risky, volatile, and uncertain world marked by accelerating climate change, along with rapid social and societal change. We would further add that explicitly referencing the economic benefits of good stewardship in the definition ensures alignment with the government's top priority of boosting growth and embedding the FRC's growth duty.

In a roundtable discussion with senior internal audit executives from Code signatory firms, participants reinforced the importance of retaining a clear mandate for addressing ESG-related risks within the Stewardship Code. There was widespread concern that removing these references could weaken stewardship expectations, leading to inconsistencies in how firms interpret and apply their responsibilities. The senior internal audit executives from Code signatory firms that we spoke to noted that this could create uncertainty for investors and signatories alike, particularly at a time when regulatory expectations for ESG issues are increasing rather than decreasing. As one Chief Audit Executive from a Code's signatory firm put it, "*Nothing seems to be consistent, and so it's confusing for investors. It's confusing for people who are trying to implement these requirements, and this is just another example where we're setting yet another expectation that doesn't align with other things that we've been asked to comply with.*"

This proposed revision of the definition coincides with the internal audit functions of Code signatory firms playing an increasing role in stewardship oversight. Internal auditors in signatory firms play a role in

[1] **Risk In Focus 2025, Chartered IIA**
[2] **Why ESG initiatives need a solid economic foundation, World Economic Forum, January 2025**
[3] **Investors want to hear from companies about the value of sustainability, McKinsey, September 2023**

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independently assessing sustainability risks and stewardship practices. The proposed revised definition does not fully reflect how stewardship oversight has evolved, nor does it align with the increasing emphasis on ESG assurance within Code signatory firms based on the discussions we have had with senior internal audit executives.

Stakeholders expect stronger—not weaker—stewardship commitments, particularly as financial regulators and global initiatives reinforce ESG disclosure requirements. Many major investment firms remain committed to sustainable investment. Schroders recently secured a £6.3 billion sustainable investing mandate, reflecting the increasing demand for ESG-integrated investment strategies. Alex Tedder, Co-Head of Equities at Schroders, highlighted this expectation shift:

"Clients, investors and the industry are increasingly focused on bespoke investment solutions that are able to deliver strong risk-adjusted returns together with a comprehensive commitment to sustainability. Our broad-based capability and commitment to active management puts us in a strong position to meet client objectives in a rapidly transforming investment environment." ESG Today[4]

This reflects a growing industry expectation that sustainability remains a core part of long-term value creation, contradicting the weakening of ESG references in the revised Code.

The revised definition moves in the opposite direction to other regulatory developments, such as the Financial Conduct Authority's (FCA) Sustainability Disclosure Requirements (SDR), which introduce stricter criteria for how investment products can be labelled as 'sustainable' and the EU's Corporate Sustainability Reporting Directive (CSRD), which strengthens sustainability reporting requirements. This inconsistency risks making it more difficult for firms to align their stewardship activities with both UK and international regulatory requirements. Additionally, The Chartered IIA's Internal Audit Code of Practice [5]explicitly recommends that internal audit functions consider including environmental sustainability, climate change risks, and social issues within their audit plans. This reflects the growing prominence of these risks and reinforces the need for strong governance and oversight, making the removal of explicit ESG references in the revised Stewardship Code, particularly concerning.

An example of the revised Code pulling in a different direction is the FCA Consumer Duty. This aims to promote transparency and comparability in investment decision-making, ensuring that investors can make well-informed choices. However, removing ESG elements from the Code could weaken investors' ability to assess and compare how firms integrate ESG considerations and weaken transparency across the funds they offer to investors. As one participant in our roundtable discussion highlighted, *"(On changes to the definition) You end up not having comparability, so your investors and clients are going to be trying to work out what these terms mean for this product versus another product. That goes completely against what the FCA is trying to create from a transparency and comparability perspective under Consumer Duty."* The revised Code risks placing investors in a worse position by reducing clarity on how ESG factors are considered within

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[4] **Schroders Wins $6.3 Billion Sustainable Investing Mandate from SJP, ESG Today,14/01/25**
[5] **Internal Audit Code of Practice Principles on effective internal audit in the financial services, private and third sectors, Chartered Institute of Internal Auditors, 2024**

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stewardship activities, at a time when regulators are reinforcing expectations for clearer, more standardised reporting.

The existing definition of stewardship remains appropriate, providing clarity, consistency, and alignment with global regulatory trends. The revised definition removes explicit references to the economy, environment, and society. Given the rising prominence of ESG risks, regulatory alignment concerns, and clear demand from investors for sustainable stewardship, the FRC should retain the current definition.

Q2. Do you support the proposed approach to have disclosures related to policies and contextual information reported less frequently than annually? If yes, do you support the approach set out above?

The Chartered IIA supports the FRC's proposal to review Policy and Context Disclosures every three years, with updates only needed annually for significant changes. With signatories already required to produce detailed annual Activities and Outcomes Reports, this is a welcome change that appropriately reduces the reporting burden for signatory firms. This proposal was met with a clear consensus among the members and stakeholders we have engaged with on the revised Code, who all agree that this change is a positive step in reducing unnecessary administrative reporting tasks.

From an internal audit perspective, this change allows the function to better allocate resources to assure the accuracy, completeness, and effectiveness of stewardship activities and outcomes, rather than expending time and effort on the Policy and Context Disclosures.

We believe, along with our members and stakeholders, that the focus of reporting should be on a meaningful and outcomes-driven basis. As long as transparency is maintained through the ongoing submission of Policy and Context Disclosures, stakeholders will continue to have access to relevant information. The move towards a more flexible reporting framework recognises that organisations should prioritise demonstrating stewardship effectiveness focussed on activities and outcomes.

Q3. Do you agree that the Code should offer 'how to report' prompts, supported by further guidance?

The Chartered IIA supports the inclusion of the 'how to report' prompts and additional guidance within the Code. Clear reporting prompts can help ensure high-quality and comparable reporting across signatories while reducing ambiguity in how stewardship is reported. This is particularly important given the diverse range of organisations that apply the Code, each with varying approaches and levels of expertise in stewardship reporting.

However, we are concerned by the removal of the references for the need for Code signatory firms to report on what internal and external assurance they have received in relation to stewardship. Its absence in the revised Code weakens transparency and accountability, creating uncertainty around how signatories will now demonstrate that stewardship processes are being independently reviewed. If explicit assurance requirements are not retained within the main Code – which would be our strong preference, then clear reporting guidance must ensure that signatories continue to uphold robust oversight mechanisms through internal and external assurance.

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Q7. Do the streamlined Principles capture relevant activities for effective stewardship for all signatories to the Code?

Internal and external assurance

The Chartered IIA does not support the removal of references to internal and external assurance for stewardship processes and practices in the revised UK Stewardship Code because assurance is essential for maintaining transparency, accountability, and robust governance. The 2020 Code rightly recognises assurance as a key mechanism for maintaining trust, ensuring independent oversight, and driving good stewardship. Under Principle 5, signatories were expected to explain:

- *How they review their policies to ensure they enable effective stewardship*
- *What internal or external assurance they have received concerning stewardship*
- *How they have ensured their stewardship reporting is fair, balanced, and understandable*

The revised Code removes these explicit references, raising concerns about how signatories will demonstrate that their stewardship processes, policies, and activities are robust and effective in the absence of defined assurance expectations. Internal audit, board-level oversight, and external assurance currently play a role in helping firms demonstrate the effectiveness of their stewardship processes, practices and activities.

Furthermore, the 2020 Code explicitly acknowledged internal audit as a form of assurance within its Principle 5 guidance:

"Internal assurance may be given by senior staff, a designated body, board, committee, or internal audit and external assurance by an independent third party."

We believe that this explicit reference to internal audit should be preserved in some form in the revised Code. Internal audit provides an independent assurance of the stewardship practices within firms.

This change is also inconsistent with the broader UK governance framework. The FRC's UK Corporate Governance Code (Provision 29) requires boards to assess and declare the effectiveness of risk management and internal controls. This recognises and demonstrates the importance of assurance at the corporate level. However, removing assurance references from the UK Stewardship Code creates a contradiction—if companies are required to evaluate internal controls and provide assurance at the corporate level, why should stewardship activities not be subject to similar assurance expectations?

Similarly, members at our roundtable discussion highlighted that asset managers place considerable emphasis on internal and external assurance processes in relation to stewardship, as these mechanisms help demonstrate robust governance and investor accountability. Removing these expectations risks weakening transparency and sends mixed signals about the importance of independent oversight as a fundamental component of good stewardship. One Senior Audit Executive noted: *"I think it's actually quite confusing to the market because asset managers spend as much time explaining in the public domain what internal and external assurance they have actually done today, and then to take that away, I think seems a little odd."*

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A clear requirement for Code signatory firms to explain what internal and external assurance they have received concerning stewardship is essential to ensure accountability and drive continuous improvements in stewardship practices. Without explicit assurance expectations, this could weaken independent oversight and reduce the quality of stewardship activities. At our roundtable, a senior internal audit executive from a major asset management firm sums up our view on this removal: *"It seems to be completely in the wrong direction to what other parts of our governance framework in the UK are asking for*."

Escalation Principle

Additionally, the Chartered IIA does not support the removal of the standalone principle of escalation in the revised UK Stewardship Code. Escalation has always played an important role in stewardship, ensuring that signatories take appropriate action when significant issues arise. The revised Code proposes embedding escalation within broader stewardship practices rather than treating it as a stand-alone principle. This risks reducing its prominence and creating inconsistencies in how signatories approach escalation.

During our roundtable with senior internal audit executives from Code signatory firms, concerns were raised that this removal represents yet another watering-down of the Code. Stakeholders viewed this as a retrograde step that could weaken accountability. Without clear reference to escalation as a defined principle, there is a risk that signatories will deprioritise or interpret escalation inconsistently, potentially leading to weaker stewardship outcomes. As one Chief Audit Executive from a major asset management firm put it: *"I think it's another watering down—I think this is a retrograde step."* Given that other regulatory bodies are reinforcing investor responsibility and governance expectations, this change could lead to an inconsistent regulatory approach, as well as weaken the Code's effectiveness in driving meaningful engagement.

The removal of explicit references to internal and external assurance and the escalation principle reflects a wider watering down of key elements of the UK Stewardship Code, leading to a weaker Code overall. A lack of assurance around stewardship practices and processes could lead to asset managers making poor investment decisions that do not fully consider long-term risks. This could contribute to lower returns for people's savings, investments, and pensions, ultimately negatively impacting the wider economy and long-term economic growth. Additionally, the absence of assurance could harm the reputation of the UK's financial markets, as investors might perceive the UK market as less committed to high standards of stewardship. For the Code to remain effective and aligned with the evolving expectations of clients, beneficiaries, investors and global regulatory standards, it must retain a clear focus on these essential aspects of good stewardship. Internal and external assurance and escalation are important mechanisms for ensuring transparency, accountability, robust oversight, and safeguarding long-term value creation for investors.

Q8. Should signatories be able to reference publicly available external information as part of their Stewardship Code reporting, recognising this means Stewardship Code reports will no longer operate as a standalone source of information?

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We support allowing signatories to reference publicly available external information, as it reduces duplication and improves efficiency. However, it is essential to ensure that the UK Stewardship Code report remains a clear and cohesive resource, avoiding over-reliance on external references that could fragment understanding and reduce the importance and value of reporting on the Code.

Q9. Do you agree with the proposed schedule for implementation of the updated Code?

We agree with the proposed implementation schedule, which provides signatories sufficient time to adapt to the updated Code. However, before publication in 2025, we strongly advocate for the reinstatement of references to internal and external assurance, as these are fundamental to ensuring accountability and robust stewardship practices. We also recommend revisiting the definition of stewardship to include explicit recognition of societal and environmental benefits, reflecting the broader responsibilities and priorities of modern stewardship. Additionally, the removal of escalation as a stand-alone principle risks reducing its importance and prominence. We urge the FRC to retain the principle on escalation to reinforce the need for strong accountability and engagement mechanisms.