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FAO: Nick Read, Chief Executive Officer
CC: Owen Woodley, Deputy Chief Executive Officer

Proposed changes to Internal Audit governance arrangements

Dear Nick,

I am writing to you as your Internal Audit co-source service provider to share our concerns on the proposed changes to Internal Audit's governance arrangements – specifically, Internal Audit reporting into the Group Assurance Director alongside the organisation's second line assurance functions.

Internal Audit plays a critical role in enhancing an organisation's ability to serve the public interest. Through the provision of independent risk-based and objective assurance and advice, Internal Audit helps to create, protect and sustain organisational value. This is of crucial importance to the Post Office given its society-led purpose and the focus placed on good corporate governance through the ongoing Public Inquiry.

The independent positioning of Internal Audit is a key principle under the Institute of Internal Auditors' (IIA) current Global Internal Audit Standards ("the Standards"), which guide the worldwide professional practice of internal auditing. Under this principle, the board is responsible for enabling the independence of the Internal Audit function, which is defined as the freedom from conditions that impair the function's ability to carry out its responsibilities in an unbiased manner. The new IIA Standards, effective January 2025, include a domain focused specifically on the responsibilities of the Chief Audit Executive (CAE), in collaboration with the board and senior management, in governing the Internal Audit function, which reiterates the importance of the board and senior management in championing the function's recognition throughout the organisation. This is driving higher levels of governance and positioning of Internal Audit activities and reporting. Internal Audit is most effective in fulfilling its role when the CAE reports directly to the board and is positioned at a level within the organisation that enables it to discharge its services and responsibilities without interference.

Further, the revised Internal Audit Code of Practice ("the Code"), which is currently in draft and will be applicable to corporates once finalised, continues to move in the direction of travel set by the Financial Services sector. The Code states that Internal Audit should be independent of risk management, compliance, finance and other control functions, and be neither responsible for, nor a part of, them. These proposed governance arrangements are not in conformance with the draft Code on the basis that Internal Audit will have the same reporting line as the organisation's second line assurance functions.

Whilst it is understood from my recent conversation with the Audit, Risk and Compliance Committee (ARCC) Chair that these new governance arrangements may be temporary, during which time the ARCC Chair will maintain a direct link to the CAE, they do not align with the Standards or the draft Code and we believe they will adversely impact the effectiveness and independence of Internal Audit and governance at the Post Office. We are also concerned that positioning the Internal Audit function alongside second line assurance functions will diminish Internal Audit's profile within the Post Office and could be seen to dilute the importance placed on Internal Audit within the organisation.

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We are already starting to see the proposed new reporting line pose challenges for planned Internal Audit work. Specifically, there is an independence challenge over the audit of the New Branch IT (NBIT, Horizon Replacement Programme) assurance plan, which forms part of the 2024/25 Internal Audit Plan that was approved by the ARCC in March 2024. Given the NBIT assurance plan was developed and is overseen by the second line and the Group Assurance Director, Internal Audit feels that its independence is compromised due to the proposed new reporting line.

We would be grateful if you can respond to this letter to explain the rationale for these changes and why you consider the proposed governance arrangements to be appropriate. We have also written to Simon Jeffreys as the ARCC Chair to share our concerns.

Yours sincerely

The GRO logo, featuring the letters "GRO" in a bold, sans-serif font, enclosed within a dashed rectangular border.

Carol Murray
Deloitte LLP