

# Internal Audit Report

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Sponsor: Jane MacLeod

Meeting date: 29 January 2019

## Executive Summary

### Context

The purpose of this paper is to update the Committee on the PO Internal Audit activity and key outcomes. This includes details of the work completed since the last Audit, Risk and Compliance Committee (ARC) meeting in October and progress on the 2018/19 Internal Audit Plan.

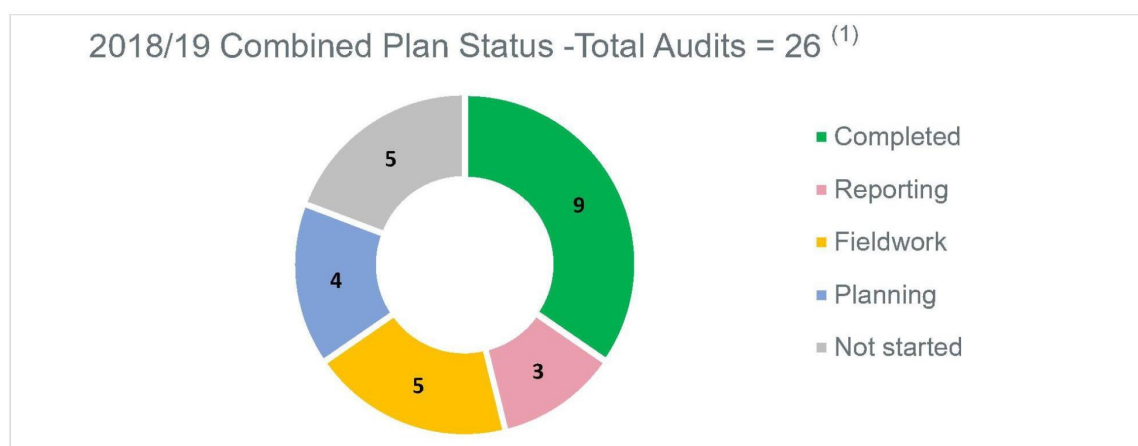
### Questions this paper addresses

- Is the Internal Audit Plan on track? What progress has been made since the last meeting?
- Do Internal Audit have adequate resources to deliver the Audit Plan?
- What progress is being made with completion of audit actions?
- Have any significant issues arisen that the committee should be aware of?

### Conclusion

#### 1. Progress against plan:

Following the appointment in October of Deloitte as our new co-source provider, and successful recruitment of the two team vacancies, we are now making good progress with delivery of the 2018/19 audit plan. We have finalised five audits since the last ARC meeting in October. At the time of writing this report three audits were in reporting with a further five in fieldwork. Current delivery progress is as follows:



<sup>(1)</sup>ARC approved baseline plan for 2018/19 (16 internal control reviews & 10 change assurance reviews).

A full summary of the 2018/19 audit plan status is included in **Appendix 1**.

**2. Open and Overdue Audit Actions (as at 21 January 2019):**

<b>Audit Action Status:</b>	
Open (not yet due)	26
Overdue (<60 days)	0
Overdue (>60 days)	0
<b>Total</b>	<b>26</b>

More detailed information is provided in paragraph 15 of the report.

**3. Significant Issues:**

Following the mid-year review of the audit plan, we proposed to the ARC that the total number of audits be reduced from 26 to 22. This was done to compensate for the delays caused by the transition to the new internal audit co-source provider as well as internal vacancies. However, the ARC expressed their concerns about a number of audits that we wanted to postpone, four of which were linked to the delayed implementation of the Back Office Transformation Programme. The committee requested that we complete the audit plan in full to provide assurance that controls over key processes are still effective in the interim period. The committee accepted that this would require additional co-source support, which is estimated to be £72k (net of savings from staff vacancies).

There are no other significant issues we believe the committee should be made aware of.

**Input Sought**

The Committee is asked to note and provide comment as necessary.

## The Report

### Changes to plan since October ARC meeting

4. The re-prioritised plan approved by the ARC is attached as appendix 1.

#### Core Internal Audit:

5. The following audits have been re-instated at the ARC's request:

- Agents Remuneration – Assess interim controls;
- Client Settlements – Assess interim controls;
- Payroll – Do a full audit;
- Procure to Pay – Review the key controls once the remedial actions from the procurement fraud investigation are complete. The current schedule and progress with remedial actions may result in this audit being deferred to Q1 of 2019/20.

6. The following audit was added to the plan at management's request:

- Network and SGEI Reporting (including Network Subsidy).

#### Change Assurance:

7. We provide assurance over Post Office's change portfolio through a dynamic programme of change assurance reviews, which includes thematic (governance) reviews as well as reviews of individual programmes. This approach was approved by the ARC in March 2018 with a target of 10 reviews for 2018/19.

8. The audit programme is being reviewed and updated on an ongoing basis to reflect the programmes most deserving of independent assurance, predominantly 'Platinum' projects. The portfolio has been under review since August 2018 with a number of initiatives being re-assessed. This has led to some being delayed (Digital Identity) while others were cancelled (i.e. Closed Cash) or are still under review (i.e. Payment Technology Upgrade). Other initiatives have been re-scoped, changing their significance and risk profile, and we are currently assessing whether a review should still be done (i.e. Mails On-line).

9. As a result of this continuous re-assessment, we have made the following changes to the programme (for a full list of change assurance reviews refer to appendix 1):

- Removed Closed Cash as project was cancelled.
- Added a review of the Deployment of One Best Way (the updated change methodology delivered by the Change Excellence programme (prev. Trafalgar)).
- Added programme review of 'P2C Belfast Exit' (moving data storage from the Belfast data centre into the Azure Cloud). We are assessing the nature and timing of a review of this significant programme. Estimated total programme cost will be £37m - £46m with predicted benefits of £12.5 - £15m. Current RAG status is amber.

### Resourcing

10. Internal Audit is now fully resourced. The two remaining vacancies were filled in November:

- Charlotte Webster joined the team as the internal audit manager for Financial Services and Telecoms. Charlotte will also be the designated Chief Internal Auditor for POI.
- Jonathan Acres was appointed as senior IT auditor.



## POMS Audit Plan

11. POL Internal Audit is also responsible for delivery of the audit plan for Post Office Insurance (POMS). Progress with the 2018/19 audit plan is reported at the POMS ARC. Three of the five audits on the plan are now complete or underway:

- Insurance Distribution Directive (IDD) - Readiness Review (Complete)
- Oversight of Appointed Representatives (Complete)
- Nemesis Project - Programme assurance (Fieldwork)

## Internal audit reviews completed

12. Since the October ARC meeting we have finalised the following five reviews:

- Employee Expenses
- Whistleblowing Process
- Month-end Close Process
- Investment Funding Controls
- Procurement Fraud Investigation

Our findings and observations are summarised below (the full reports are available in Diligent's reading room):

Employee Expenses (Ref. 2018/19-02)									
<div>Unacceptable</div>	<p>An audit of employee expenses was scheduled for 2018/19. An employee fraud, identified in March 2018, identified potential abuse of Corporate Procurement Cards (CPCs) and as a result management requested that the audit be accelerated and for controls over procurement cards to be included in the scope.</p>								
<p><b>Sponsor:</b> <i>Al Cameron / Mo Kang</i></p>	<p>The audit was initially undertaken from May to July 2018. At the time of clearing the draft report in October 2018, management requested that we undertake further work to investigate unusual purchases made through procurement cards.</p>								
<p>Audit actions:</p> <table border="1"> <tr> <td>P1</td><td>6</td></tr> <tr> <td>P2</td><td>1</td></tr> <tr> <td>P3</td><td>0</td></tr> <tr> <td>Total</td><td>7</td></tr> </table>	P1	6	P2	1	P3	0	Total	7	<p>We would like to highlight that management have pro-actively taken steps to improve the controls over employee expenses and CPCs before the start of this audit, however, they recognised that more work was required and believed that an audit would support them to quickly address control weaknesses. The audit identified a number of significant control weaknesses that exposed PO to the risk of fraud, error and non-compliance. As a result we assessed the control environment at the time of the audit as '<b>unacceptable</b>'.</p>
P1	6								
P2	1								
P3	0								
Total	7								
	<p>Specifically we have identified the following control themes that required urgent remediation (remedial actions were rapidly implemented, even while the audit was still underway):</p>								
	<ol style="list-style-type: none"> <li>1. Policies not fit for purpose, or in need of improvement (for Travel &amp; Expenses, Gifts &amp; Hospitality and CPCs).</li> <li>2. The quality assurance process for employee expenses was not replicated when the new system was implemented in January 2018. This was not an omission, but an operational decision discussed at GE. Anomalies and errors found by the audit confirmed the need to re-instate independent checking and validation.</li> </ol>								



	<ol style="list-style-type: none"><li>3. Incorrect configuration when Selenity was implemented in January 2018 resulted in expense claims for Group Executives not being reviewed and approved by a person of appropriate seniority or delegate.</li><li>4. There was no requirement or process for receipts to be submitted for CPC transactions.</li><li>5. The audit findings highlighted the need for a programme of training and/or increased awareness for employees regarding the compliant spending of company funds.</li></ol> <p>We emphasise that no instances of fraud or wilful abuse were found (we tested a representative sample, including data analytics of 100% of 12 months' transactions). At the time of writing this report, 3 out of the 6 P1 actions were already complete, with the remaining 3 P1 actions on track for completion by 28 February. It is our view that completion of these actions will significantly reduce the risks identified by the audit.</p>
<p><u>Management Comment provided by Al Cameron</u></p> <p>When the Paul Swanton fraud was identified I said to the ARC that controls over employee expenses had not yet been prioritised on our controls agenda, as we focused on financial reporting and IT. Given the identification of a material fraud, I felt we had to accelerate our assessment and while we would normally prefer to review and fix before an audit, in this case it would be helpful to get an audit assessment straight away.</p> <p>The audit has taken longer than planned because I asked for additional work to give us more clarity and evidence on whether other fraudulent behaviour had taken place. That has been done and I would like to thank the internal audit team for their hard work.</p> <p>There is no evidence of fraud and that is positive. The Finance Directors get data on and review travel spend to ensure it is at a sensible level and we are not losing material cost savings.</p> <p>As we expected, the control environment was not strong enough and there was widespread non-compliance. Angela was already reviewing the expenses policy and some of the areas where we were non-compliant were logical and we have acknowledged that by changing specific elements of the policy.</p> <p>We had previously taken out a team checking receipts and asked individuals and their managers to take responsibility. That hasn't been working well and we have re-instituted some sample checks in HRSC.</p> <p>The availability of Corporate Credit cards had previously been reduced but at the time we could not institute the right controls under the provider contract. We have now been through the process to identify a new provider, with controls in place and the service is currently in transition.</p> <p>This has been a helpful review that has enabled some rapid improvements.</p>	

Whistleblowing Process (Ref. 2018/19-11)									
<p><b>Satisfactory</b></p> <p><i>Sponsor:</i> <b>Jane MacLeod</b></p> <p>Audit actions:</p> <table border="1"> <tr><td>P1</td><td>0</td></tr> <tr><td>P2</td><td>3</td></tr> <tr><td>P3</td><td>2</td></tr> <tr><td>Total</td><td>5</td></tr> </table>	P1	0	P2	3	P3	2	Total	5	<p>The objective of this audit was to assess the design and operating effectiveness of the controls over the Whistleblowing process. The audit assessed the following scope areas:</p> <ul style="list-style-type: none"> <li>Governance arrangements.</li> <li>Staff awareness and understanding.</li> <li>Managing whistleblowing concerns.</li> <li>Management information and reporting.</li> </ul> <p>The audit concluded that the Whistleblowing process is well managed by the Financial Crime Team and monitoring and reporting has been improved since they assumed responsibility a year ago. Further improvements highlighted by the review, will help ensure that Post Office colleagues have confidence to use the process when appropriate. The three P2 findings relate to:</p> <ul style="list-style-type: none"> <li>Absence of a mechanism to confirm and measure staff awareness of the whistleblowing arrangements and to gauge the success of awareness campaigns.</li> <li>No targeted training provided to staff who are responsible to investigate whistleblowing reports.</li> <li>Lack of root cause analysis and action plans to address recurring cases.</li> </ul>
P1	0								
P2	3								
P3	2								
Total	5								
<p><u>Management Comment provided by Jane MacLeod</u></p> <p>Post Office takes seriously its obligations to provide a safe and confidential framework within which whistleblowing reports can be made. The improvements identified by the audit are helpful and will be addressed to ensure that all Post Office employees and those others to whom the policy applies, feel able to report instances of wrongdoing or other behaviours which do not meet Post Office's standards.</p>									
Month-end Close Process (Ref. 2018/19-12)									
<p><b>Satisfactory</b></p> <p><i>Sponsor:</i> <b>Al Cameron</b></p> <p>Audit actions:</p> <table border="1"> <tr><td>P1</td><td>0</td></tr> <tr><td>P2</td><td>1</td></tr> <tr><td>P3</td><td>2</td></tr> <tr><td>Total</td><td>3</td></tr> </table>	P1	0	P2	1	P3	2	Total	3	<p>An audit of the Month-end Close process was originally scheduled for 2019/20 as part of the 3-year rotational audit programme of core processes. However, the audit has been brought forward to the current year in response to the issues experienced with the reporting of Telecoms revenue at the 2017/18 year-end.</p> <p>The objective of this audit was to assess the design and operating effectiveness of key controls over the Month-end Close process, including balance sheet &amp; control account reconciliations, accruals &amp; provisions, journal processing and finance director review of the balance sheet.</p> <p>We conclude that the Month-end processes are operating effectively and the control environment has been further strengthened to ensure accurate representation of the financial position. We have therefore rated this audit '<b>satisfactory</b>'.</p> <p>We further note that since the introduction of the Financial Controls Framework programme in 2016/17 there has been continuous improvement on the monitoring and reporting of the Month-end Close Process with increased attention since the 2017/18 year-end.</p>
P1	0								
P2	1								
P3	2								
Total	3								
<p><u>Management Comment provided by Al Cameron</u></p> <p>Good to see the progress made and we will take forward the helpful additional actions.</p>									

**Investment Funding Controls** (Ref. 2018/19-16)

Needs  
Improvement

**Sponsor:**  
*Rob Houghton*

Audit actions:

P1	0
P2	4
P3	1
Total	5

UKGI have raised concerns over the robustness of Post Office's oversight and control of the Strategic Plan's implementation and accuracy of the quarterly progress reports in support of funding draw downs. Internal Audit were asked to review and assess the key portfolio level processes and controls, including those governing the reporting of progress and funding.

Management have previously recognised that significant improvement is required to improve the maturity and effectiveness of controls over its change portfolio. A series of initiatives, both short term tactical and long term strategic, were set in motion through the Change Excellence programme (previously called Trafalgar). Nonetheless, this review highlighted further areas for improvement:

- Process and control inefficiencies in the management of programmes at portfolio level;
- Roles and Responsibilities not clearly defined; further improvements required to ensure effective monitoring of programmes at portfolio level;
- Current benefit modelling and reporting is not appropriate for programmes delivered under an Agile methodology.

The audit also identified some deficiencies in the controls over the preparation of the quarterly report to UKGI, particularly with regard to cost and benefit forecasts. The noted deficiencies had a minor impact on the Q3 report, however, we emphasise that the report was not materially impacted by these weaknesses and we confirm the accuracy of reporting of actual cost.

We have rated this report '**Needs Improvement**' as there are some process and control weaknesses that, if not addressed, may result in inaccurate reporting in future.

Management Comment provided by Rob Houghton

The challenges on change delivery were already recognised and a programme established to improve controls, transition to agile method and improve delivery. The audit was commissioned in the middle of this work. This audit is therefore timely as the incremental improvements identified are already added to the scope of the work.

**Procurement Fraud Investigation** (Ref. 2018/19-03)

Not Rated

**Sponsor:**  
*Al Cameron*

Audit actions:

P1	4
P2	0
P3	0
Total	4

Post Office have experienced a significant, systematic, employee fraud, committed by a senior person in a position of trust (total value in excess of £300k). Management requested that Internal Audit conduct an investigation to understand the control failures that have allowed this fraud to take place. One element of the fraud (to the value of £49k) was committed through the company's procurement process, hence this investigation focused on the controls around the purchase to pay process.

We conclude that the individual was able to commit this fraud by abusing his seniority and level of trust within the organisation and by colluding with a supplier. He is being prosecuted for his activities and has cooperated fully with the investigatory work.

Some inherent weaknesses in the current process and outdated procurement system have contributed to the fraud being committed and not being detected. Replacing the system was not an IT priority,



	<p>however, management have recognised the risks associated with the current system and this is reflected in the Post Office risk analysis. Management is currently looking at options to replace the outdated procurement system, which will significantly improve the control environment. As an interim measure, management have agreed to additional actions (some already completed) to further mitigate the risk of similar fraud being committed. We have no reason to believe that other instances of fraud took place.</p> <p>This was a specific piece of work, targeted on the fraud. As the work was investigatory in nature the report has not been rated. The investigation will inform a more comprehensive review of the procurement process, which is scheduled for Q4 2018/19 or Q1 2019/20.</p>
<p><u>Management Comment provided by Al Cameron</u></p> <p>This was a helpful review and it is positive that no further instances of fraud have been identified. As we know our controls over procurement have been limited by the legacy systems. We have been working for some time on a replacement system, with a RFP on design and cost already in the market. The decision to invest may well rest on the control benefits as the pure financial case may be limited.</p>	

### Reviews in Progress

13. The following reviews from the 2018/19 audit plan are in progress:

	<b>Review</b>	<b>Status</b>	<b>Fieldwork</b>
1	Contract Management (IT)	Report being drafted <sup>(1)</sup>	15/10 - 09/11
2	Agents Portal (Change)	Report being drafted <sup>(1)</sup>	08/10 - 31/10
3	Opening of Bank Accounts	Report being drafted	05/11 - 11/12
4	Cyber Security Maturity Assessment	Fieldwork (Ph. 1 complete)	07/01 - 29/01
5	Financial Control Framework	Fieldwork	07/01 - 31/03
6	Client Settlements	Fieldwork	10/12 - 31/01
7	Agents Remuneration	Fieldwork	07/01 - 08/02
8	Network and SGEI Reporting	Fieldwork	23/01 - 22/02

<sup>(1)</sup> Reporting delayed by availability of staff over December and resources being re-prioritised in favour of the Investment Funding review.

### Reviews in Planning

14. The following reviews from the 2018/19 audit plan are being planned for delivery in Q4:

	<b>Review</b>	<b>Status</b>	<b>Fieldwork</b>
1	Payzone Integration (Change)	Planning	Feb
2	Mails Strategy (Change)	Planning	Feb
3	Payroll	Planning	Feb
4	IT Control Framework	Planning	March

**Updates on Internal Audit Open and Overdue Actions**

15. Audit actions are generally being completed on time. At 21 January there were 26 open actions, with no actions overdue.

<b>Audit Action Status:</b>	<b>BAU</b>	<b>Change</b>	<b>Total</b>
Open (not yet due)	19	7	<b>26</b>
Overdue (<60 days)	0	0	<b>0</b>
Overdue (>60 days)	0	0	<b>0</b>
<b>Total</b>	<b>19</b>	<b>7</b>	<b>26</b>

END OF REPORT

**Appendix 1 – Re-prioritised Plan** (As agreed with ARC on 30 October 2018)

<b>2018/19 Internal Audit Plan - Status as at 21 January 2019</b>					
<b>No.</b>	<b>Title/Subject</b>	<b>Sponsor</b>	<b>Notes</b>	<b>Timing</b>	<b>Status / Rating</b>
<b>Internal Control Reviews</b>					
1	Product Risk Review (Postal Orders)	O. Woodley	Original	April	<b>Needs Improvement</b>
2	Employee Expenses	A. Cameron / M. Kang	Original	April	<b>Unacceptable</b>
3	Procurement Fraud Investigation	A. Cameron	<b>Addition</b>	May	<b>Not Rated</b>
4	Month-end Close Process	A. Cameron	<b>Addition</b>	Nov	<b>Satisfactory</b>
5	MoneyGram Compliance	O. Woodley	<b>Addition</b>	Sept	<b>Satisfactory</b>
6	Contract Management (IT)	R. Houghton	Original	Oct	<b>Draft Report</b>
7	Whistle-blower Process	J. MacLeod	Original	Oct	<b>Satisfactory</b>
8	Opening of Bank Accounts	A. Cameron	<b>Addition</b>	Nov	<b>Draft Report</b>
9	FS Training & Competence	O. Woodley / M. Kang	Original	March	Not Started
10	Cyber Security	R. Houghton	Original	Jan	<b>Fieldwork</b>
11	IT Control Framework	R. Houghton	Original	March	<b>Planning</b>
12	Financial Control Framework	A. Cameron	Original	Jan	<b>Fieldwork</b>
13	Payroll	M. Kang	Original	Feb	<b>Planning</b>
14	Client Settlements Process (Interim Controls)	A. Cameron	Original	Jan	<b>Fieldwork</b>
15	Agents Remuneration (Interim Controls)	A. Cameron	Original	Jan	<b>Fieldwork</b>
16	Network and SGEI Reporting	D. Smith	<b>Addition</b>	Feb	<b>Fieldwork</b>
17	Procure to Pay	A. Cameron	Original	Q4 / Q1	Not Started
18	Branch Cash Forecasting & Management	A. Cameron	Original	Q1 19/20	<b>Postpone<sup>(1)</sup></b>
19	Supply Chain Management	A. Cameron	Original	Q1 19/20	<b>Postpone<sup>(1)</sup></b>
20	Digital Strategy & Capability	O. Woodley	Original	2019/20	<b>Postpone<sup>(2)</sup></b>
21	Online Sales	O. Woodley	Original	2019/20	<b>Postpone<sup>(2)</sup></b>
22	Data Privacy (GDPR Follow-up)	J. MacLeod	<b>Addition</b>	Q1 19/20	<b>Postpone<sup>(2)</sup></b>
<b>Change Assurance<sup>(3)</sup></b>					
1	Change Programme Governance (Trafalgar)	R. Houghton	Governance	May	<b>Advisory Report</b>
2	DMB Strategy	D. Smith	Programme	July	<b>Satisfactory</b>
3	Agents Portal	D. Smith	Programme	October	<b>Final Draft Report</b>
4	Investment Funding Controls	R. Houghton	Governance	November	<b>Needs Improvement</b>
5	Payzone Integration (Panther)	D. Smith	Programme	Jan	<b>Planning</b>
6	Digital Identity Services	M. Edwards	Programme	Feb	<b>Planning</b>
7	Mails Mobile App (Tracked Online)	D. Smith	Programme	TBC	Being re-assessed
8	Payment Technology Upgrade (PCI)	D. Smith	Programme	TBC	Being re-assessed
9	Mails Strategy	D. Smith	Programme	TBC	Being re-assessed
10	One Best Way Deployment	R. Houghton	Governance	March	Not Started
11	P2C Belfast Exit	R. Houghton	Programme	TBC	Being assessed

<sup>(1)</sup> Delay until after BOT programme is complete and new controls embedded.<sup>(2)</sup> Postpone due to process still bedding down and maturing (GDPR) / restructuring (Digital & Online).<sup>(3)</sup> The list of Change Assurance reviews was approved by the ARC on the basis of being the highest risk programmes planned for 2018/19 at the time. The list is being reviewed and updated on an ongoing basis to reflect the programmes most deserving of independent assurance, predominantly 'Platinum' projects.