

Post Office Ltd – Strictly Confidential**RISK AND COMPLIANCE COMMITTEE****22 March 2006 – Meeting Ref 08****Members:**Sir Mike Hodgkinson (Chair)
Peter Corbett
Ian Anderson**In Attendance**Rod Ismay
Keith Woollard**Apologies**

Alan Cook

SUMMARY ACTION POINTS

ITEM	ACTION	LEAD
0801	"Fraud and control" to be a formal agenda item at the next meeting, and to include the implications of different methods of payment. Done. Included in draft agenda for 6 September (in covering email)	Rod Ismay
0802	Irrelevant	
0803		
0804		
0805		
0806		
0807		
0808	Brief Ian O'Driscoll on Legal Services issues meetings to date Done. Briefed Ian and he is taking forward with Director of Legal Services	Rod Ismay
0809	Irrelevant	
0810	Following appointment as Managing Director, Alan Cook to resign from this Committee.	Rod Ismay

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1. MINUTES FROM LAST MEETING

Meeting Ref 07 - minutes approved.

Irrelevant

2. STATUS OF ACTIONS FROM THE PREVIOUS MEETING

ITEM	ACTION	LEAD
0701	Irrelevant	
0702		
0703		

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0704	Irrelevant	
0705	<p>Analyse 80 branches with largest shortages revealed at audit to identify if the shortages came as a surprise to Service team personnel.</p> <p>Current year audits with shortages > £25k were reviewed:</p> <p>During this 11 month period, there were 32 such audits of which 6 (19%) were prompted by concerns raised by Service. As Service had not raised any concerns for the remaining branches, it would indicate that the financial results of audits are a surprise in over 80% of cases.</p>	<p>Martin Ferline</p> <p>Closed</p>
0706	Irrelevant	
0707		
0708	<p>Update IMPACT audit report for progress up to end of period 11 before further circulation.</p> <p>RI to give update at meeting.</p>	<p>Rod Ismay</p> <p>Closed</p>
0709	<p>Update Royal Mail Internal Audit & Risk Management with the committee's observations on the list of potential areas for audit in 2006/07</p> <p>Done. IA&RM agreed that relevant programmes to consider for audit would be the initiatives arising from Rainbow, not Rainbow itself.</p>	<p>Rod Ismay</p> <p>Closed</p>
0710	<p>Advise Rod, by exception, of any issues re Investigations note</p> <p>No further comments received.</p>	<p>Committee members</p> <p>Closed</p>
0711	<p>Defer "Audit Charter and Third Party Audit Requests" to next meeting</p> <p>Agenda item at next meeting.</p>	<p>Rod Ismay</p> <p>Closed</p>

Brought Forward From 8 November 2005

ITEM	ACTION	LEAD
0605	<p>Update Committee on outcome of Branch Audit Half Year Report recommendation concerning ownership and analysis of cash data.</p> <p>Ultimate owner agreed as Peter Corbett. Additional MI activity within the current "Retail Inventory" team in Operations is explained in Appendix 3 to the briefing pack for the March Committee and responds to a recent series of cash losses in February and March 2006.</p> <p>Following OD (Organisational Design) changes to cash ownership will be addressed by new responsibilities within Finance.</p>	<p>RI</p> <p>Ongoing</p>

Post Office Ltd – Strictly Confidential**3. MATTERS DISCUSSED AT THE MEETING AND NEW ACTIONS REQUESTED**

The issues discussed included the following items (which are expanded on as shown):

- 3.1 Actions from previous meetings
- 3.2 IMPACT project status
- 3.3 Method of payment for products in branches
- 3.4 Business control
- 3.5 Updates and plans from Branch Audit and from Investigations
- 3.6 Regulatory compliance
- 3.7 Year end group reporting – risks and controls
- 3.8 Third party audit requests and audit charter

3.1 Actions from previous meetings

All actions brought forward were agreed as closed with the exception of:

0605 Management information – longer term ownership and prioritisation to be addressed within OD

Irrelevant

3.2 IMPACT project status

Peter submitted a status report to the Royal Mail Audit & Risk Committee (ARC) in March. The ARC noted the report and did not raise any questions.

Post Office Ltd recognises there are open issues with the new systems and that Ernst & Young (external audit) have concerns for the imminent year end, but that action plans are in place to ensure auditable accounts for the year end and longer term solutions in the new year.

The Committee had previously challenged on 3 broad areas. Status updates at the meeting were:

- Data to support and enhance fraud identification – significantly improved since the last meeting but still not fit for routine usage, such as in the Branch Audit Risk Model. For business accounts purposes adjustments are being made to underlying finance records, but due to the issues in the underlying data it has not been practical to load it into risk models. Pre-existing data feeds continue to raise significant branch issues. It should be possible very soon to use the new data.
- Management Information – as noted by the Director of Sales at the Leadership Team meeting on 21 March high quality daily MI has now become available to the business. However, there are important strands of MI which are not being delivered yet such as bureau de change data. The issues blurring the data are now more clearly understood and "fixes" are being progressed with urgency.
- Auditability of accounts – whilst there are very material adjustments being made to the underlying finance balances, there are clear plans in Product & Branch Accounting to deal with these for the year end.

Rod presented a short audit report on the project status, attached at Appendix A. This noted the key themes of concern for the year end audit and the outline of P&BA's plan.

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3.3 Method of Payment for Products in Branches

It was noted that there is concern in some parts of the business about cheques. There is a risk of fraud and counterfeiting of cheques as a method of payment (as well as the separate risk of counterfeit DWP cheques being presented for encashment in branches). Cheques may also have higher administrative costs than other methods of payment such as debit cards.

Opportunities were considered which might bring benefit to the business, its clients and its customers, for instance incentives such as £25 discount on another product if the customer paid by debit card instead of cheque and possibly coupled with surcharges to the customer should a cheque be used and bounce.

Action 0801

"Fraud and control" to be a formal agenda item at the next meeting, and to include the implications of different methods of payment.

Action 0802

Quantify the costs associated with cheques as a method of payment (including administration, re-presentation, settlement terms).

3.4 Business Control

The Committee considered what else might be done, assuming a clean sheet, to reduce fraud risk. Suggestions included:

- Tight recruitment and robust exit processes.

- As reliability of data improves post-IMPACT, a review of branches regularly featuring in the Branch Audit Risk Model and a requirement for constructive evidence as to why they should not be considered for corrective action and possible termination of contract.

- Controlled support channel for branches being maintained open after suspension of former subpostmaster, by use of interim subpostmasters and the Service Project Pool.

- Activity under the future area badged "Director for the Protection of Surrounding Post Offices".

- Aligning accountability (as with compliant sales) right through the job descriptions post OD.

- Positive backing of the "winning branches" to incentivise the right behaviours.

- Fast focussed response to MI

- Product simplification and rationalisation

- Enabling branches to get it "right first time"

Action 0803

Align accountability through job descriptions and performance measures post OD (as has been done with "Compliant Sales" already) and ensure the support and tools to do it are available.

Action 0804

Network Director to be invited to report to this Committee twice a year.

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3.5 Updates and Plans From Branch Audit and From Investigations

A recent spate of high value branch losses was noted (5 incidents from £30k to £82k since the last Committee meeting). The highest related to a community post office considered small and which consequently received small fixed cash remittances without review. Such branches have now been built into the Retail Inventory Team's Flexible Planning System.

The Branch Audit plan for 2006/07, which had been presented to the preceding Committee meeting, was formally endorsed.

The Investigations brief was noted with no comments arising.

3.6 Regulatory Compliance

The Regulatory Compliance brief was noted with no comments arising.

3.7 Year End Group Reporting – Risks and Controls

The draft group reporting papers were noted. Rod is to subsequently brief Alan Cook on these papers, as business unit Managing Directors are now expected to sign off such half yearly returns.

Action 0805

Advise Ian of outstanding self assessments on HR related key controls.

Irrelevant

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4. AOB

Rod raised three additional topics from a corporate governance perspective:

Information Security resource – The IS Officer is shortly to retire and it is understood that outsource is being seriously considered. Rod suggested that in Post Office Ltd's markets it may be expected that the company would retain at least the qualified resource to supervise the outsource provider, if not to retain the whole activity.

Legal Services resource – Rod outlined the external shift in legal resourcing and the current issues in oversight of legal relationships. Ian noted the appointment of Ian O'Driscoll to coordinate legal relationships going forward.

Irrelevant

Action 0807

Obtain brief and advice from Post Office Ltd Operations Directorate as to Information Security options inhouse in POL, inhouse in Royal Mail Group and outsourced.

Action 0808

Brief Ian O'Driscoll on Legal Services issues meetings to date.

Irrelevant

Action 0810

Following appointment as Managing Director, Alan Cook to resign from this Committee.

5. DATE OF NEXT MEETINGS

Wednesday 6th September 2006	-	10.30 - 12.30
Thursday 7th December 2006	-	10.30 - 12.30

Post Office Ltd – Strictly Confidential**Appendix A – Audit Report on IMPACT Status**

To Post Office Ltd Risk & Compliance Committee
CC Head of Product & Branch Accounting

From Rod Ismay, Head of Audit & Risk
Date 22 March 2006

Executive Summary

IMPACT and the POLFS accounting system have moved on significantly since the last report to the Risk & Compliance Committee.

The system is not yet processing all transactions correctly and so the end state of POLFS ledgers which automatically interface to the main business accounts (ESFS) has not yet been achieved. However, manual adjustments can and are being made to the ledgers for the year end.

The adjustments include several mis-postings which individually are very large, but which in most cases are substantiated. Where full substantiation has not yet been provided there is clear ownership to ensure that they are evidenced for the year end.

The external audit is well underway. Given the tight timescales, Ernst & Young are understandably nervous about the year end. However, POL Finance are in close dialogue with them, and E&Y are constructively supporting Finance by bringing:

- (a) Additional urgency, clarity and prioritisation to the auditability of the accounts, and
- (b) By raising the questions and potential solutions which are compensating for capability shortfalls in some areas of the business.

The key themes which underlie this area are as follows and are consistent with E&Y's understanding:

- 1) Systems response times which make some accounts difficult to open and hence need manual adjustments. Fixes are being progressed with PRISM around "housekeeping".
- 2) Gaps in accounts ownership and/or ability to explain balances coherently. The material accounts at stake have been identified and are being progressed with all urgency.
- 3) Incomplete reconciliations of accounts and from POLFS to ESFS at previous period. An approach has been agreed to deal with this for the year end.
- 4) Accounting and supervisory capability issues. These are being managed for the year end on a directive basis but will be addressed in the new year as part of Finance Development.
- 5) Visibility of interface controls – ie to confirm completeness and "once & once only".
- 6) Some specific accounts raised as concern by E&Y and internal review including bureau de change, Camelot income and "client vendor payment clearing". Owners are agreed here.

There has been very significant progress in systems functionality, accounting processes and certain people's accounting awareness since January. A number of "mis-mappings", data interfaces and "clearing routines" have been dealt with. However, as explained above several adjustments will continue to have to be made at period ends into the new year.

Proposed Year End Process to Resolve Current Issues – As Proposed by P&BA to E&Y

Having clarified the issues from period 11, there will now be a 2 stage year end:

1. An interim period end will happen as of Wednesday night. POLFS effectively gives "real time" accounting for the network and so should be equally meaningful and auditable at any date. Balances will be run as at Wednesday and overlaid with the known adjustments. POL then has 2 days to perform a final healthcheck before the year end.
2. The final year end accounts closure will happen as of Sunday night. The "adjustments" run at Wednesday will in some cases be the same. A full accounts interface supported by full ledger reconciliations will be done as at the year end.

Accounts evidence will include detailed account reconciliations and third party evidence where possible such as Branch Audit evidence of cash balances and routine bank reconciliations.