

Australia General Construction, Inc.

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TEACHING CASES 2020

Introduction

John Richmond, a thirty-eight-year-old with a degree in Construction Engineering with a MBA, is the Chief Audit Executive (CAE) of Salmon Creek Engineering and Construction LLC (SCE&C). SCE&C is listed in the New York Stock Exchange, and it operates on a global scale in the large infrastructure industry, with General Contracting, Project Financing and Operation & Maintenance Divisions. John became the Chief Audit Executive since few months, after working for four years in a large international auditing company and following for about two years as Controller of a medium-sized construction company.

It was a quite Friday afternoon and John started to plan his weekend making order on his desk when the phone rang. The CEO's assistant told him that Robert Marshall (CEO) needs to meet him immediately. When John entered in the CEO's office, the CEO went immediately to the reason for the meeting. "Dear John" he began "you have been with us for a few months and we are very happy with how you are working. The position of CAE is covered by a person who does not limit himself to verifying that "the procedures are respected" but that is able to make a contribution to the achievement of our strategies". "For this reason," Robert continued, "I would talk about an ambitious and reserved project that we have for our expansion abroad. As you know the SCE&C's objective, in the execution of our worldwide strategy as per 2019 - 2022, is to enter into the Australian market. With the aim to minimize environmental and market risks, we have been looking for potential acquisitions of an existing company (M&A). After a very careful analysis of possible target firms, the choice is going towards the Australia General Construction, Inc. (AGC)."

The Australia General Construction, Inc. (AGC)

The CEO handled a report about the AGC showing that it is a family company totally owned by the founders. It operates in technological infrastructural projects, like hospitals and industrial buildings. At the moment, it is involved in one significant construction project through a SPV (special purpose vehicle), the AGC- EPC (Engineering, Procurement, Construction) Dam Project. The owner of the project is LPP Energy (a provincial crown corporation under the Government of Queensland). The company is also running for several initiatives in New Gales regarding the transport industry. Moreover, the AGC is the sole owner of another Australian Construction Company, Fast Track Construction (FTC), which is executing several little residential buildings projects. Projects are generally managed through specific Special Purpose Vehicles (AGC-EPCs).

The Role of the Internal Audit of SCE&C

In case of possible acquisition, SCE&C gives assignment to a primary audit company to be financial advisor for the operation performing also all due diligence activities. In this situation, the top management of the company believe that a due diligence based only on financial approach is not sufficient. AGC is very different from SCE&C in relation to mission, ownership and governance and it is necessary to conduct a wider due diligence not limited to financial issues. The due diligence of a third party based only on financial aspect is weak. When there is a value creation perspective, the reasonable sustainability of this project is evaluated through other aspects starting from the adequacy of the governance of the company, as risk management and internal control are the pillars of a sound corporate governance.

The first step of this process is our understanding of the “as is” situation in relation to how AGC is managed in term of structures, process and procedures, with a focus on risk and control governance. The analysis of the “as is” situation should be not limited to a “bureaucratic” approach: it is necessary to fully understand how risks are identified, managed and controlled in AGC.

The engagement plan (work program) for AGC due diligence

Because in a M&A transactions the acquiring company needs to reduce the probability of surprises and should be aware and anticipate risks there are several issues that should be dealt with in order to mitigate the risk of the low performing acquisition. These issues are in relation to:

- values, vision and mission;
- formalized processes for values creation;

- disciplined approach for risk management and internal control, in order to ensure that the interests of all stakeholders (including SCE&C) are protected;
- differences in processes, policies, procedures, competencies, know – how, risk appetite between SCE&C and AGC that make the integration process longer, more expensive and riskier.

Therefore it is necessary to perform a due diligence to consider all these aforementioned risk factors. The way John Richmond decided to conduct the due diligence is trying to find an answer to the following questions:

- What is the AGC business model, how it operates?
- Has AGC a clear understanding of its objectives and related risks, including strategic, operational, compliance risks?
- What are the specific risks and opportunities that affect the organization’s ability to create value over the short, medium and long term, and how is the organization dealing with them?
- How does the organization’s governance structure support its ability to create value in the short, medium and long term?
- Is the Risk & Control Governance of ACG suitable, considering its context and pre-defined evaluation criteria?

Analyzing these dimensions and answering these questions mean that SCE&C is going to perform a specific due diligence on Enterprise Risk Management (ERM) and Internal Control System (ICS) of AGC. This due diligence should be based on international best practices using the COSO Framework. John Richmond has to decide how to conduct such assessment, when there was not a-priori information about the structure, processes and procedures of both the Enterprise Risk Management and Internal Control Systems. Moreover, it is not sufficient to have a static view of these systems but obtain a clear understanding how they are put in place and made effective. As a consequence, the aim of the assessment is not only the appraisal of the System “per se” according to a formal perspective. It is necessary to assess if there is a sound and effective risk management and internal control system because it provides a reasonable assurance that the company is well managed.

This activity is part of the entire due diligence process that covers other aspects and risks (financial, compliance, legal, business, etc.). At the same time neglecting any considerations on these characteristics might not result automatically in an un-successful integration but it represents an underestimation of the risks related to the organization of the target company.

This due diligence consists of several phases:

- A. An analysis of the context. We should gather information on AGC corporate structure and organization (See *annex n° 1*). This preliminary analysis also aims to identify the key-process owners to interview.
- B. The Control & Risks Self Assessment (CRSA) is aimed to collect basic data and information on ERM and ICS system of the target company. CRSA will be made with interviews: the engage-

ment consists of an independent assessment of the fundamental components of Internal Control Integrated System (as known as Entity Level Controls), using as reference and benchmark CoSO Report ICS Guidelines:

- a. Control Environment – The focus is on standards, processes and structures that provide the basis for carrying out IC across the three different organizations. Have they similar risk and control culture? Which is the commitment to Values, Ethics, Accountability and Competence? Are there any differences in term of risk appetite?
 - b. Risk Assessment – The analysis is on the maturity level of risk management processes, which involves a dynamic and iterative process for identifying and analyzing risks to achieving entities' objectives. Have been all risks identified and managed? Could Risk Management process of target company be aligned to the strategy of AGC?
 - c. Control Activities – Policies and procedures are integral parts of the Integrated Management System to help ensure that directives to mitigate risks related to the achievement of objectives are carried out. How much are they formalized, implemented and communicated? How feasible and quick could be the shift to a unique management system?
 - d. Information and Communication - Focus here is on reporting system. The effort needed to integrate it could be very time-consuming. The audit will concern: existence and compatibility of an internal and external, financial and not – financial reporting system; Information flows to Governance Bodies; Management of external communication.
 - e. Monitoring – Ongoing evaluations, separate evaluations, or some combination of the two are the review activities that make any system resilient to change. The focus here is on the assurance system of target company, using as a benchmark the 3 Lines of Defense Model, in order to evaluate its reliability and avoid excessive redundancy.
- C. After each interview, we will develop and submit to the process owner for approval a Memo of Meeting – MOM (NDR: See *annex n° 2*)
- D. With all the MOMs on hands, we will have sufficient information to finalize the Entity Level Controls Questionnaire (NDR: See *annex n° 3*) that will be our interim report to be discussed with the Management of the target company in order to agree upon findings and recommendations.
- E. The Entity Level Controls Questionnaire will be the basis for our conclusions and general opinion that will be included into the Executive Summary (NDR: See *Annex n° 3*) in which we will summarize the final judgement as part of the overall due diligence to be presented to Top Management and Board of SCE&C”.

In order to finish the job on time John asked to be supported by a team of two young internal auditor (George and Geraldine) from the audit department of SCEC. First task of his staff was to prepare the audit plan in the form to collect information in order to perform phase 2) and 3) of the job scheduled”.

“I like your program”, Robert said, “and I will provide you with the needed budget. So let’s go and be quick!!”.

The preliminary survey

As planned, John contacted soon after AGC senior officers (CEO and CFO) and sent them a Communication explaining the engagement program, the schedule starting from next week and requiring preliminary documentation:

- The corporate structure and highlights;
- The Organization Chart;
- The list of main policies and procedures.

Only documentation of bullets 1. And 2. was provided. But John considered it enough for identifying process owners to be involved into the CRSA workshops. He sent the interview schedule to AGC, requiring to meet following officers:

- Vincent Scott
- Ann Scott
- Daniel Fielding
- Luis De Vito

The kick-off meeting for AGC ERM & ICS due diligence (held at SCEC Headquarter)

As planned, on Monday John and his team were in Queensland in order to interview AGC management. They had very warmly reception, and people were very friendly with them. But when they sat to start up the meeting, John had impression that not all the people of AGC were so enthusiast for their presence. He may say someone very enthusiast, and someone less. As required, participants at the first meeting were:

Vincent – Ann Scott are owners of the Australian company and deal respectively with the commercial (V) and administrative (A) aspects. Although both are in favor of SCE & C's entry as the majority shareholder, Ann is more convinced of the transaction due to financial advantages (greater capitalization and less use of external lenders). Vincent fears that the shareholder may limit his discretion and influence the friendly and collaborative climate that characterizes AGC
Daniel Fielding: a young engineer hired by AGC, he is the Project Manager of the Mega project where he takes care of all aspects, under the supervision of Vincent and Ann, and maintains relations with the client. Strongly in favor of the entry of the new partner in order to favor the passage from a family management (of which Daniel suffers limits and interference) to a managerial company.

Luis De Vito: director of the FTC, the small company that deals with residential construction is also Vincent and Ann's brother-in-law. It carries out some activities in favor of AGC tendentially based on the costs incurred plus margin (cost plus commission).

After the illustration of the scope of work, John agreed the schedule of single interviews that he and his team performed during the week.

First Summary of the interview of AGC management

Regarding the interviews steps, the approach to firstly provide selected process owners with a general overview on Internal Control and Risk Management systems in order to create awareness on main standard / principles and related taxonomies; then to structure the interview in logical and ordered questioning based on a preliminary specific job assessment, without following exactly the sequence of principles and points of focus provided by relevant framework (ref. Internal Control - Integrated Framework (CoSO 2013)). The basic communications and listening techniques used during the interviews were:

- to pay attention about what is said and how the communication is carried out;
- to develop empathy with interviewee through active listening and nonjudgmental questioning;
- to be objective, interested and respectful;
- to make open questions, avoiding self response questions;
- to avoid being aggressive or reacting negatively in case of negative/uncooperative attitude;
- to reflect on what is says, summarize and/or rephrase on answers
- to encourage interviewee to ask relevant questions

At the end of the week all the interviews were completed and the “first picture” of ERM & ICS system, by component of the selected framework, was summarized into specific Memos.

John was satisfied of the job made by him and his team. According to him now there were sufficient details to start the fulfillment of the Entity Level Controls Questionnaire.

But it was clear to him that in order to close the interim report and the executive summary and corroborate the conclusions and general opinions a lot of hard job had to be done and, maybe, more interviews to other levels of AGC organizations. Probably he had to spend another week end working, with his team.

Annex n. 1 – AGC Organization

Corporate Structure: From 2017 the structure, organization, head office personnel and relative costs of all AGC-EPCs have been absorbed by AGC which is therefore the holding company for commercial and bidding activities in Australia. AGC have acquired sole control over FTC and with its head office structure ensure direction and coordination on all the AGC Group.

Main sectors / markets Current activities are focalized on Business Development, with a focus on complex and larger infrastructure projects, including DBF (Design, Build, Finance) and concession projects. Followed market are Social Infrastructure, Power/Environment, Transport, Private Sector.

Ongoing Projects: One mega project is directly performed by AGC, with a special purpose vehicle – SPV (AGC-EPC Dam Project); other residual projects are managed with ad hoc special purpose vehicle

Main Clients: LPP Energy (a provincial crown corporation under the Government of Queensland) is the owner of the Mega project and main client of AGC;

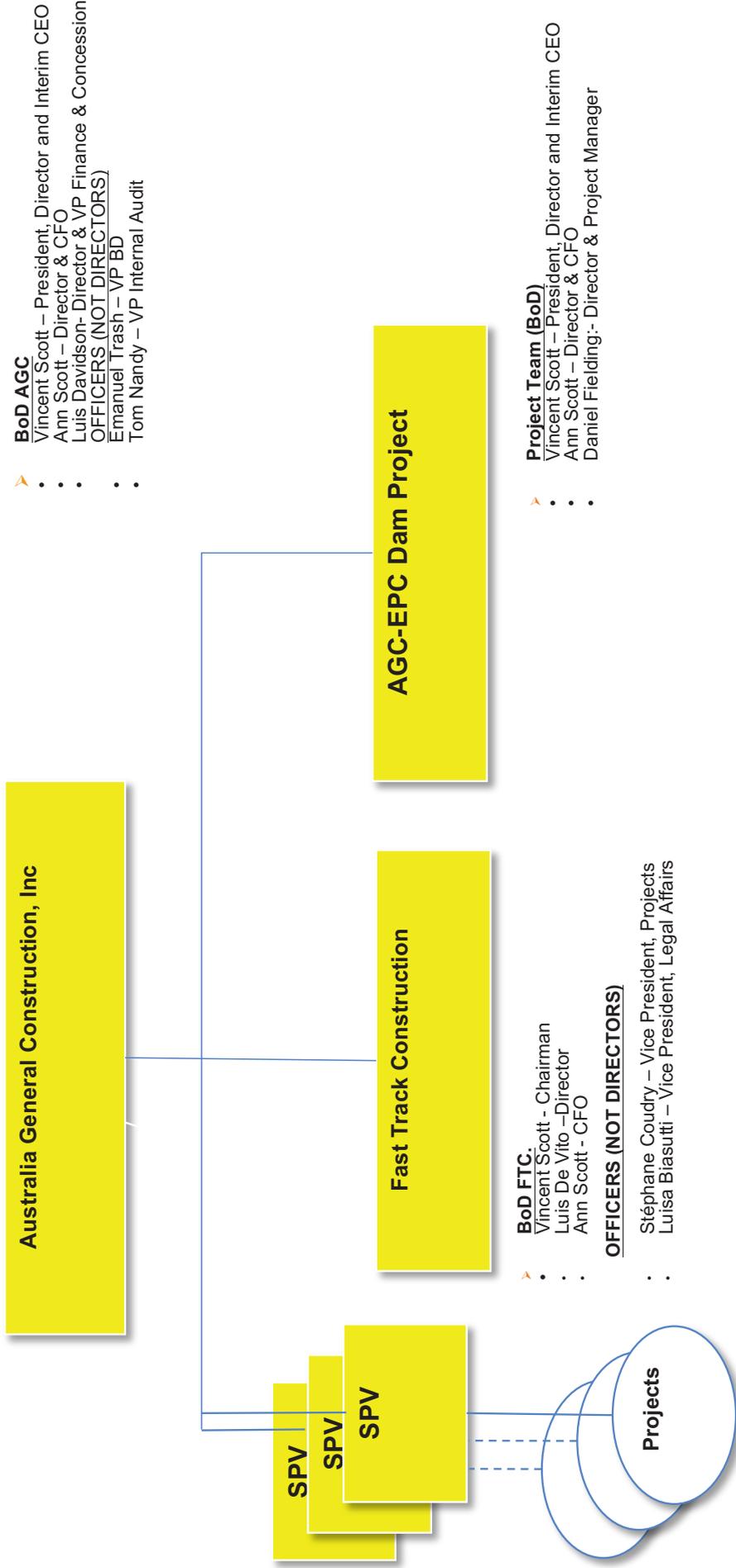
On-going Tender & Acquisition: Future Outlooks will be formalized with the approval of 2019 AGC Business Plan. The target company o is currently developing several initiatives in New Gales regarding the transport industry

General Purpose Subsidiaries: AGC has the sole control over another Australian Construction Company, Fast Track Construction (FTC), which is executing several little residential buildings projects.

Updated Operative Backlog: 800 mln <\$>, with a residual technical life of 4 years, without new acquisitions

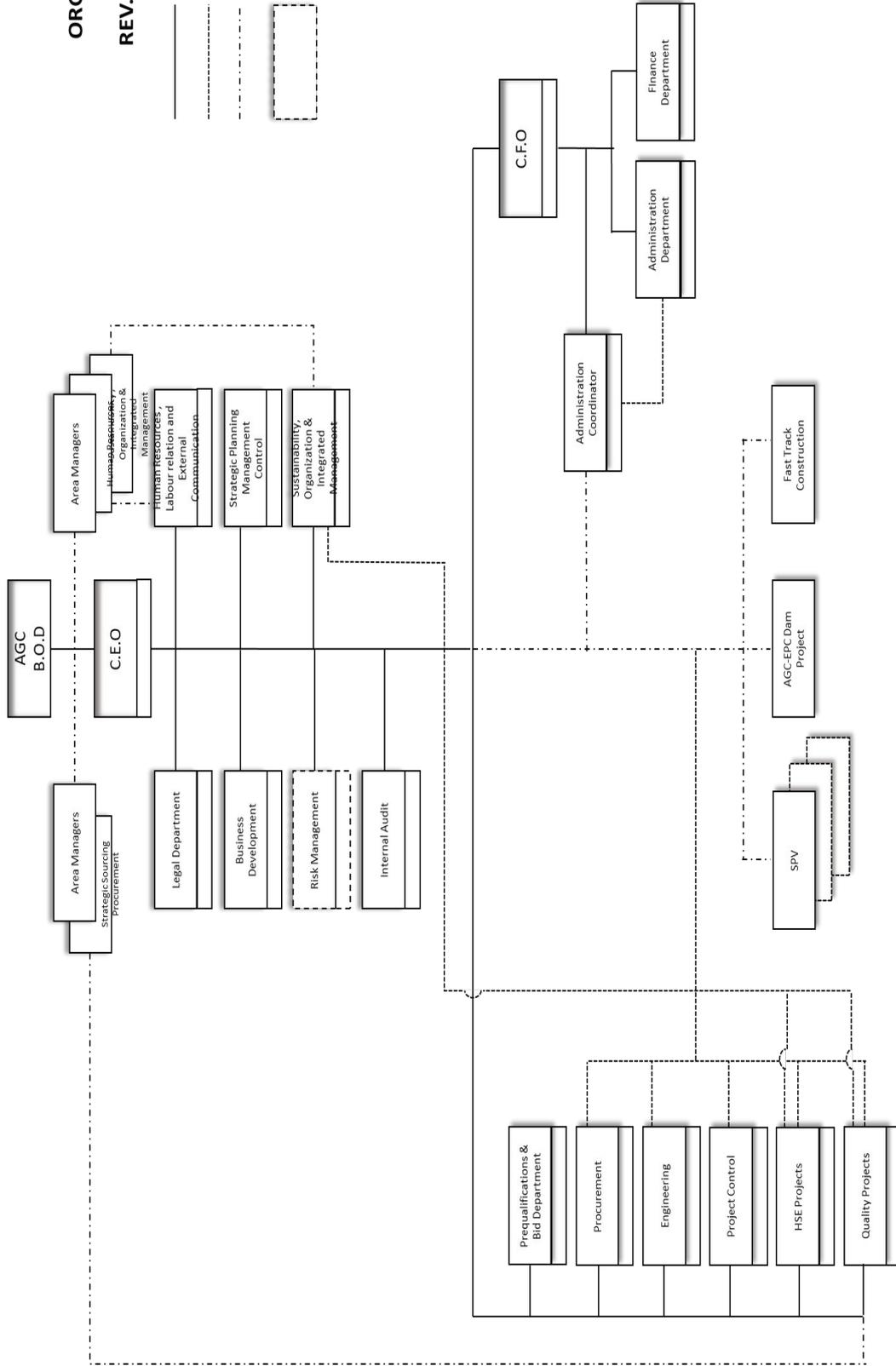
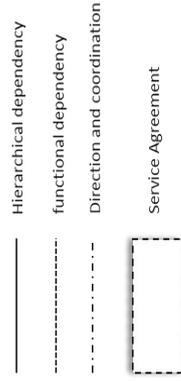
Yearly production: 200 mln <\$>

AGC Corporate Structure as of November 20XX



AGC Organization

ORGANIZATIONAL CHART REV. 0 - 15.11.20XX



DRAFT DOCUMENT

Annex n. 2 – MOMs

Below are the minutes of meeting (MOMs) prepared by John and his team after each interview

Interview n. 1

**MOM
Information Gathering
AGC – IC Due Diligence**

Queensland, Monday

Process Owner: Vincent Scott - Owner, Chairman and CEO, Focus on General and Operation Management and Business Development

Audit Team: John Richmond (Accountable and Supervisor), **George Michael and Geraldine Schiavone**, Auditors

Flash Report – Highlights

General Aspects

- Corporate Governance of AGC is clearly defined into Company’s Bylaw according to Australian Law. The responsibilities for strategic direction and oversight (including control oversight) is on the board of directors, but the oversight of the development and performance of internal control is exercised informally (no specific mention into BoD charter, no topics on Risks, Controls, Ethics, Compliance Program in the agenda of BoDs and related resolutions).
- According to the Corporate Structure as of November 2017, ABC Boards consists of 5 Directors (including the Chairman and Interim CEO - Vincent), which can represent the Company.
- BoD retain authority over significant decisions, review management’s assignments, approves the budget, reviews financial statement estimates and interacts with external auditors, but the organization structure (Organization Chart) has not been defined / approved by the BoD neither at enterprise or at departmental level.
- Vincent totally agree that there is the need to establishment of formal AGC management system, including powers and limitations of authorities
- According to Vincent, there is a serious weakness related to common missions and objectives. AGC is changing, new employees with different backgrounds have be hired and, because of a lack of deep induction on AGC policies and procedures that are not formalized, most of AGC employees don’t have common “know-how” and don’t share same values and principles. That’s

why, before SCE & C started initiative, Vincent was already planning to develop a project aimed to improve:

- Tone at the top
- Leaderships
- Values awareness
- Risk and control culture

Anyway such project has not started yet.

- Regarding to structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives, Vincent has confirmed that the organization structure is still unofficial, mainly with reference to:
 - Operations
 - Finance
 - Concession and Structured Finance
- In particular, for mentioned department roles and responsibilities formalized into a clear Job Description Handbook. During the interview we analyzed with Vincent and collected into engagement work papers the unofficial company organization chart has not been formally issued. We analyzed the draft of the Organizational Chart, not yet approved: this draft doesn't indicate the managers of each department. Moreover doesn't include the organization under Finance & Concessions. With respect to this point, Vincent highlighted that there are still discussion with Ann Scott in order to clarify organizational position and reporting lines of Finance & Concessions Team (including interfaces with Headquarters). There are two alternatives they are evaluating Decisions on the operating model for concession & structured finance:
 - To leave it into the legal structure of AGC, or;
 - To incorporate these activities into a specific legal and management structure, reporting to Relevant central Function.
- In both cases, Finance & Concession organization chart and roles must be formally defined
- Regarding to authorities and responsibilities (including PoAs and Delegations) the current situation is not under control, according to Vincent:
 - Legally the company is represented by its directors; Vincent as Chairman and CEO as general PoA and is the legal representative
 - Anyway, the Company has also 7 officers (non directors): for some of these (in particular for recently appointed VPs) there is not evidence of the BoD resolutions or POAs which are needed to define delegation of signing authorities and limitations, but they are acting on behalf of the Company
- When we asked Vincent if AGC has a formal authorities, approvals and responsibilities matrix he had no idea about it

Focus on Business Plan, objectives setting and risk management

- Objectives (with a focus on Business & Area Development) are clearly defined into the AGC Business Plan and included into the Industrial Plan. Performance is monitored on a on-going basis, with monthly updating. Strategic Planning and Management Control is based on not formalized procedure and developed with dedicated sw/systems
- The BoD is working on a risk appetite statement in order to align strategy setting and risk. In particular, for New BD Opportunities / Acquisitions / Projects Selection (as documented into the Business Plan, Acquisition Plan, and SAPO /ASPO Forms for each bid) there is always a preliminary objectives and related risk assessment
- There are not formal risk management processes, mainly at enterprise level. For instance, Vincent was trying to convince the BoD on the appointment of a Risk Manger, but no decision has been made;
- Risk management is more mature at project level, because of specific contractual requirements with the client;
- With the exceptions of mentioned areas, Risk Management is managed with a unformal and scattered silo based approach (in term of risk identification, analysis, and response)

Managerial reporting and monitoring

- Most of the information senior management use derive from the Strategic Planning and Management Control, and related systems, which have been developed in line with local best practices.
- Anyway at the moment there isn't any consolidated monthly management report at ABC / Country level (ie. Monthly / Quarterly General Report). Management reporting is focused on current project and project based

Interview n.2

MOM
Information Gathering
AGC – IC Due Diligence

Queensland, Tuesday

Process Owner: Ann Scott - Director, CFO

Audit Team: John Richmond (Accountable and Supervisor), George Michael and Geraldine Schiavone, Auditors

Flash Report – Highlights

General Aspects

Considering roles and responsibilities of Ann, her interview has been focused on compliance and administrative aspects, starting always from current Company Governance. She highlighted that:

- Among her duties, she acts as general secretariat of the Board of Directors, organizing the agenda of meetings. Board meetings are biweekly and Board meets with senior management every month in order to get information on the status of operations and outlooks. For every Board meeting there is a detailed agenda and MoMs, approved by the Director
- The composition of the Board of Directors has not changed since several years. There are not independent and non-executive directors. Ann considers this reasonable, because of the current capital structure, company by-law and the aim to protect the sole shareholder's interests. Regarding conflict of interest management, principles are provided only by the Code of Ethics. In terms of relevant expertise, Board members have multidisciplinary expertise.
- AGC adopted a Code of Ethics. The AGC website includes information on the Code of Ethics, but any details are provided on the company mission and values
- Ann is aware of Mission and Vision Statements and Corporate Values (Fairness, Safeguarding Assets, Professionalism, Sustainability) of SCE & C and she thinks that could be very important for AGC to adopt and formally communicate similar Mission and Vision to all employees;
- An Ethics Officer with the duty of evaluating adherence to expected standards has been formally nominated by the Board of Directors, but the extent of its vigilance is very limited. For instance, there is not any hotline (even anonymous) directly connected to the Ethics Officer e-mail address in order to report any misconduct and employees have not been informed regarding the possibility to communicate to the ethics officer
- The disciplinary system linked to the Ethics Compliance Program is not working at all and according to Ann there are needs of improvement in order to effectively implement ethical standards;

- Some improvements we discussed with Ann are:
 - To communicate the Ethic Program (meaning the existence of an hotline) to Company Personnel
 - To establish a Cross-Functional Ethic Committee in order to evaluate any deviation from the Ethic Principles. This committee (usually composed by HR, Finance and Legal internal Experts. could oversight the compliance with the Ethic Code, helping the Ethic Officer in accomplishing its duties.
- Ann agreed with such improvement opportunities
- Regarding the management system (policy and procedure), Ann reported that:
 - there is a draft of a General Policy on Quality, Health & Safety and Environment (Sustainability Policy) and AGC is going to formalize its own management system (IMS). After reading the General Policy for Sustainability of SCE & C, she convey that AGC should adopt similar Policy and Procedure ensuring in future consistency with SCE & C's Sustainability Model and Policy
 - there is a project aimed to develop written policy and procedure according to ISO International Standards. The manager of Quality Assurance Dept has been just appointed. The new department is leading the implementation of such management system (Integrated Management System), but at the moment all IMS Documentation (including: Policy, QHSE Manual, OrgChart, JD Handbook, Management Procedures, etc) are in draft version or not yet elaborated. There is plan of issuance for all main MP, OP & Policies (it should be finalized by the end of 2018) but there are several delays;
 - periodical management review of IMS and system performance monitoring tools have not been implemented. This is an objective for next year, after IMS issuance
- With respect of last points, we discussed with Ann on the necessity to ensure consistency between AGC and SCE & C Management System. Therefore, even if the lack of clear policies and procedures is a serious weakness of current AGC internal control system, it could be an opportunity, making quite easier the integration process. We discussed with Ann the general principles that are requires to every SCE & C according to specific Group Guidelines:
 - Traceability;
 - Segregation of Duties;
 - Formal Delegation of Authorities;
 - Existence of formal procedures, requires compliance with general procedures relating to the setting, definition and development of business management system for the entities belonging to the Group;
- Ann is quite worried about this, because current AGC system has several gaps with such standards

Focus on Business Plan, objectives setting and risk management

- According to Ann current risk management practices are basically compliance based. It means that there is not a comprehensive risk assessment, based on all companies objectives (strategic, operational, financial, reputational, etc).
- Risk assessment workshops and exercises have been done if and when required by law or contracts. For instance:
 - At corporate level there are risk assessments focused on crime risk (es. Anticorruption) and privacy, that have been used in order to establish specific compliance programs required by law (the process is still on going and there is not an Anti - Corruption Policy / Management System);
 - There is a project to initiate a Fraud Risk Assessment with the assistance of external advisors. At the moment, AGC has not adopted and implemented procedures on Anti- frauds and Ann is quite worried about this
 - IT Governance is based on COBIT standards and has been certified. Anyway most of the processes (ie. procurement, budgeting and project control, planning, etc) are not managed using dedicated systems, because a lack of personnel training and engagement;
- At project level risk assessment is more detailed:
 - For the main project there is a risk register, but the PM is updating it only annually, when it is needed for the budget
 - The project risk register doesn't include the mitigation strategy, but it encompass only a financial evaluation of the value at risk in order to post contingencies into the project budget
 - For HSE (health, safety and environment) the analysis of risk and the definition of mitigation measured is very detailed, because the client requires specific risk assessment and risk mitigation plan for every single activity into the project scope of work
 - Always at project level, PM is developing an analysis of corporate social responsibilities aspects, taking into account all the stakeholders that could affect or are affected by the mega project

Accounting System

- The AGC's accounting system and financial reports are based on International Accounting procedures
- Testing activities (financial audit) similar to SOX are performed by CFO with checklist
- Independent assurance is also provided by external auditors.
- Independent audit are not performed by an Internal Audit Department (no form third line of defense)

Human resource management

- HR Policies and Practices are formalized and consistent with Relevant general Principles
- Some AGC employees have been involved in training activities but there is not any specific and structured training program for ABC corporate staff. The onboarding process of new hired employees (including officers / VPs) doesn't encompass an induction on management systems, procedures, practices, requirements, etc..
- Ann is quite worried because several organizational changes are ongoing, starting from the decision to transfer the Head Office. These changes could affect organization integration if the objectives are not clearly communicated
- Regarding accountability management, Ann reported that performance measures, incentives, and rewards are based on predefined standards and centrally monitored. A performance evaluation process is initiated annually, in order to link compensation and other rewards to performance. Among other, performance evaluation criteria include internal control responsibilities, in order to align incentives with ethics and values
- By the other side, there are not any practices to disciplines individual in case of misconduct

Interview n. 3

MOM
Information Gathering
AGC – IC Due Diligence

Queensland, Wednesday

Process Owner: Daniel Fielding - Project Manager

Audit Team: John Richmond (Accountable and Supervisor), George Michael and Geraldine Schiavone, Auditors

Flash Report – Highlights

General Aspects

Considering roles and responsibilities of Daniel, his interview has been focused on project related aspects. He highlighted that:

- At project level objectives and related risks are well defined (i.e. Mega Project planning, budgeting and monitoring process, Project risk Management Plan (PGR) and Risk Registers);
- SoD principles are embedded into current practices and transaction control activities, mainly for main sensitive processes at project level (es. purchase-to-pay, personnel administration, treasury and finance, accounting, project control).
- However, in Daniel opinion the lack of a formalized organizational structure (in terms of not codified roles, reporting lines and responsibilities / signing authorities matrix) is resulting in situation of excessive discretionary power, confusion and duties' overlapping;
- A possible solution could be the finalization of the IMS (Integrated Management System), definition and implementation, following general principles provided ISO standards, in order to avoid incompatible functions and to map identified risks to control activities (matrices, inventory of control activities, traceability requirements)
- This is a critical success factor at enterprise and project levels, considering that the AGC main client is requiring a better project management system, including the definition of a Project Management Plan (PMP) and annexes for each project. Daniel is currently working on developing a PMP for the main AGC project but he may need a better support by corporate departments
- The lack of defined Job Descriptions (JDs) and IMS Resp. Matrix is another critical point according to Daniel: it could cause deficiencies in terms of communication of control objectives and reporting lines, considering also several organizational changes and new not-codified roles into AGC organization. Basically, Daniel would like to have clearer direction for main processes he is involved in (i.e. how to hire a new employee; which are the interested officers in case of

litigations with the clients; who can communicate officially with the client and take relevant decision regarding the contracts, etc). As AGC is a family company, all this kind of processes and decisions are managed following practices without a managerial approach

- Another area of confusion is Finance and Concessions: responsibilities are not clearly defined and allocated.
- Daniel is also worried of the integration process with FTC that is too slow. The two companies (AGC and FTC) have still different IT Systems, different budgeting and reporting systems, different approach to project management. Differences are also at cultural level, as previous FTC employees don't feel to belong to AGC group and don't share same objectives and values. This is creating several internal conflicts, that could affect business objectives

Human resource management

- Daniel is the HR management accountable for all the staff and workforce on site, for the projects that he leads. He knows that there are HR Policies and Practices at corporate level but he didn't have the change to read and learn them.
- The cause is, according to Daniel, a lack of top – down communications. He doesn't know if Company Job Descriptions Handbook has not been formally issued, as well as the other document of the IMS. Even if issued, they have not been communicated to all employees, with a specific training program: as a consequence, current reporting lines, even if known, are unofficial.
- Daniel convey that in order to defining authorities at different levels of management, RACI Matrix and Delegation of authority signing Matrix are very needed

Monitoring activities

- As PM for major AGC projects, Daniel has specific monitoring duties, as first line of defense
- According to Daniel, monitoring activities are basically performed on on-going basis by the first level of defense, with management oversight provided by Strategic Planning & Management Control Dept, Project Control and Adm & Finance Dept. Coordination and oversight activities are as well under the responsibility of Area Managers (Strategic Sourcing Procurement Coordinator, Overseas HR coordinator, Area Sustainability and Integrated Management Coordinator).
- Regarding the second level of defense, Quality Assurance Dept has been just established, but internal auditing activities on projects have not been initiated yet (they should start after the implementation of IMS and related procedures).
- With a focus on the second line of defense, there aren't any procedure on Internal Audit, Non conformances, Corrective/Preventive Actions, Management Review, neither at Corporate or Project Level

Interview n. 4

MOM Information Gathering AGC – IC Due Diligence

Queensland, Thursday

Process Owner: Luis De Vito - Director of the FTC

Audit Team: John Richmond (Accountable and Supervisor), George Michael and Geraldine Schiavone, Auditors

Flash Report – Highlights

General Aspects

Considering roles and responsibilities of Luis, his interview has been focused on organizational integration between AGC and FTC. He highlighted that:

- change management is a current critical factor, considering that:
 - a new Corporate Structure has been just finalized but not formalized
 - Parent Company is re - focalizing its Business Plan on major civil projects with a preference of DBF Contract Type. This will involve a radical change in the management approach, starting from strategic planning;
 - Instead FTC Business is very stable and steady: residential construction sector is based on costs incurred plus margin contracts (cost plus commission) and all the works are sub-contracted.
 - Current backlog is less than 40 mln \$ and the value of each contract is 5 mln \$ on average.
 - That's why FTC doesn't need a big structure, formalization and reporting system; it must be focused on basic project management.
 - This is an advantage but also a risk, because doing FTC will ensure every year the same margin (12%) without a real perspective of growth, that is needed considering the AGC Group Business plan
- Luis is not aware if AGC has any policy or procedure applicable to FTC. In his opinion such policies and procedure could be a cost and an excessive bureaucracy for FTC, because of its current organization (no segregation of duties) and operational objective (time to market):
- Therefore the process of integration of FTC with AGC is still on going and this is creating several discussions with AGC officers because they would like that FTC adopted the same management accounting and reporting system but in Luis opinion this is not feasible

Annex n. 2 – Entity Level Controls Questionnaire

Control environment					
The control environment is the set of standards, processes and structures that provide the basis for carrying out internal control across the organization. The board of directors and senior management establish the tone at the top regarding the importance of internal control and expected standards of conduct					
#	Principle	Point of Focus	Assessment	Evaluation	Recommendation
1	The organization demonstrates a commitment to integrity and ethical values:	<p>Sets the tone at the top</p> <p>Establishes standards of conduct</p> <p>Evaluates adherence to standards of conduct and Addresses deviations in a timely manner</p>	-		-
2	The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control	<p>Establishes oversight responsibilities</p> <p>Applies relevant expertise</p> <p>Operates independently</p> <p>Provides oversight for the system of internal control</p>			
3	Management establishes, with broad oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives	<p>Considers all structures of the entity</p> <p>Establishes reporting lines</p> <p>Defines, assigns, and limits authorities and responsibilities</p> <p>Establishes policies and practices</p> <p>Evaluates competence and addresses</p>			-
4	The organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with Objectives				

		shortcomings				
		Attracts, develops, and retains individuals / Plans and prepares for succession				
5	The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives	Enforces accountability through structures, authorities, and responsibilities / Evaluates performance measures, incentives, and rewards for ongoing relevance / Considers excessive pressures				
		Evaluates performance and rewards or disciplines individuals	-			
Risk assessment						
Risk assessment involves a dynamic and iterative process for identifying and analyzing risks to achieving the entity's objectives, forming a basis for determining how risks should be managed. Management considers possible changes in the external environment and within its own business model that may impede the ability to achieve its objectives.						
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6	The organization specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to Objectives	Exercises judgment in areas such as specifying suitable objectives and sub-objectives and assessing risks to achieving these objectives Considers risk appetite and risk tolerance in defining strategies and objectives Defines Compliance Objective in order to reflect external laws and regulations				
7	The organization identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed	Includes entity, subsidiary, division, operating unit, and functional levels / Analyzes internal and external factors; Involves appropriate levels of management; Estimates significance of risks identified / Determines how to respond to risks				

8	The organization considers the potential for fraud in assessing risks to the achievement of objectives	Considers various types of fraud / Assesses incentive and pressures / Assesses opportunities / Assesses attitudes and rationalizations				-
9	The organization identifies and assesses changes that could significantly impact the system of internal control	Assesses change in the external environment / business model / leadership				
<p>Control activities Control activities are the actions established by policies and procedures to help ensure that management directives to mitigate risks related to the achievement of objectives are carried out. Control activities are performed at all levels of the entity and at various stages within business processes, and throughout the technology environment</p>						
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10	The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels	Addresses segregation of duties				
11	The organization selects and develops general control activities over technology to support the achievement of objectives	---				
12	The organization deploys control activities through policies that establish what is expected and procedures that put policies into action	Establishes Policies and Procedures to Support Deployment of Management's Directives				
<p>Information and communication. Information is necessary for the entity to carry out internal control responsibilities in support of achievement of its objectives. Communications occur both internally and externally, and provide the organisation with the information needed to carry out day-to-day controls. Communication enables personnel to understand internal control responsibilities and their importance to the achievement of objectives.</p>						
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13	The organization obtains or generates and uses relevant, quality information to support the functioning of other components of internal control.	Processes Relevant Data into Information			
14	The organization internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control	Provides Separate Communication Lines			
15	The organization communicates with external parties regarding matters affecting the functioning of internal control”	Communicates to External Parties			
Monitoring activities Ongoing evaluations, separate evaluations, or some combination of the two are used to ascertain whether each of the five components of internal control, including controls to affect the principles within each component, is present and functioning. Findings are evaluated and deficiencies are communicated in a timely manner, with serious matters reported to senior management and to the board					
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16	The organization selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning	Considers a mix of ongoing and separate evaluations			
17	The organization evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the board of directors, as appropriate”	Assesses results / Communicates deficiencies / Monitors corrective actions			