



UK Government  
Investments

# **POST OFFICE LIMITED (“POL”)**

OVERVIEW

JULY 2016

## 1 SUMMARY AND KEY ISSUES

***Government is sole shareholder of Post Office Limited (POL), setting requirements which POL must meet, then allowing it to operate commercially***

***POL is loss making and relies on Government subsidy; however it is in the middle of a complex transformation programme to reduce that subsidy***

***This is ambitious but achievable, and with political support will place POL on a sustainable long term footing within this Parliament***



The Post Office network is a relatively small and discrete policy area, but one which attracts a significant amount of interest from both Parliament and the public. On one hand, Post Offices are held in high esteem as hubs of the community (particularly rural communities) providing essential services to often vulnerable people; on the other, some see them as outdated and inefficient, with the majority of their services replaced by other providers and the Internet

Government policy has tended to strike the balance between recognising the social and economic functions that the network provides, with the need for the company to operate commercially and taxpayers paying no more to support it than is necessary. Since 2010, Post Office Limited (the Government-owned company responsible for the network) has been undertaking a transformation programme, supported by Government investment, which should see the company moving towards a more sustainable long term footing within this Parliament with reduced subsidy

This pack gives a high-level overview of how POL is set up, the areas in which it operates, and its long term strategy. There are also some short term matters (below) which you need to understand and may require prompt action. We recommend you receive more detailed advice on each

**INDUSTRIAL RELATIONS (SLIDE 13):** The Communication Workers Union (CWU) which represents POL's directly-managed employees is balloting for industrial action and calling on Government to step in and halt POL's modernisation. It fears job losses and "privatisation by the back door". POL are well-placed to manage any disruption caused by strike action, but the vocal way in which the union flag their concerns may attract attention of the media and Parliamentarians

**HORIZON (SLIDE 14):** A small number of mostly former-subpostmasters have raised concerns about POL's Horizon IT system, which they claim has caused their businesses losses. Over two years' worth of independent investigation has found no systemic faults in Horizon, but campaigning and media interest persists. Civil litigation has been commenced against POL

## 2 STRUCTURE AND OWNERSHIP

***POL is one of the largest retail business in the UK with a 350 year history, operating a network of c.11,600 branches across the country***

***It was separated from Royal Mail in April 2012 and is 100% Government owned, via a holding company that also previously owned the remaining stake in Royal Mail***

***Government does not seek to influence POL's day-to-day operations***

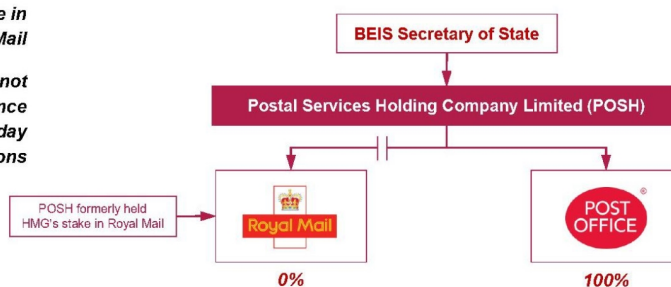
POL is a commercial business that operates independently of Government. It has a Chief Executive and a Board of Directors, who are responsible for running POL day-to-day and for providing strategic oversight, respectively

The Government owns 100% of POL, through the Postal Services Holding Company (POSH) which previously also owned the Government's remaining stake in Royal Mail. There are currently plans to wind-up POSH in early 2017 to simplify this shareholding structure

The Post Office team in UK Government Investments (UKGI) manage the Government shareholding in POL. This includes a non-executive seat on POL's Board. The Government has various shareholder rights in areas such as Board appointments, remuneration, and POL's strategic plan.

The Postal Services Act 2011 requires POL to be wholly public-owned, but allows for the move to a mutually-owned structure in the future. Any alternative structure or ownership model would require further primary legislation. Mutualisation will only be possible if POL is financially sustainable

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### 3 FUNDING

**Government funds POL to enable it to maintain a network of post offices beyond its optimal commercial size, and to make that network more efficient**

**Without support, POL would not be a going concern**

**Government has committed nearly £2bn between 2010 and 2018**

**Funding benefits POL's customers, and also helps to reduce POL's overall reliance on taxpayer support**



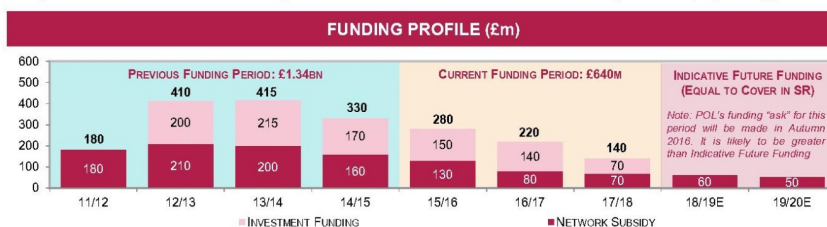
Government provides funding to POL in order to maintain a network beyond its optimal commercial size and footprint. Currently the requirement is a network of more than 11,500 branches which meets 5 clearly defined access criteria (e.g. 99% of the UK population must live within 3 miles of their nearest post office). There is a legally-binding funding agreement between Government and POL

Since 2010, Government funding for POL has been focused on two areas:

**NETWORK SUBSIDY:** Payment to maintain a network of post offices in line with Government's requirements. Recognised by POL as revenue in its accounts

**INVESTMENT FUNDING:** Funding for POL to invest in its network, to make it more efficient and less reliant on taxpayer funding. It is recognised by POL as a direct cashflow in its accounts

BEIS received SR funding cover for £60m subsidy in 2018/19 and £50m subsidy in 2019/20, which was in line with an indicative funding requirement set out by POL in 2013. Recent discussions with POL however suggest senior management have an appetite to go further with POL's transformation and as such a funding "ask" for these years might be higher than planned. It would be expected that any additional investment funding would further reduce POL's need for long term taxpayer support





## 4 FINANCIAL OVERVIEW

*Last financial year POL generated revenue of £871m which was broadly flat on 2014/15*

*Underlying operating profit (i.e. after adjusting for a £30m reduction in network subsidy) was higher by £34m, and ahead of expectations*

*POL's profitability is expected to improve further in 2016/17 although revenue is forecast to fall marginally, due to ongoing difficult market conditions*

In 2015/16 POL generated revenue of **£871m** (£1,001m including Network Subsidy) and an operating profit of **£104m**

Revenue was below budget, mainly due to underperformance in Financial Services and Other (specifically Supply Chain)

However due to tight cost control and certain one-off benefits operating profit was ahead of expectations

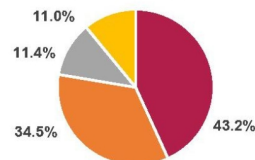
POL's most significant cost is payments made to subpostmasters – in 2015/16 **£413m** was paid out to **c.11,400** subpostmasters, a simple average of **c.£36,000** per branch

Due to Network Transformation these costs are now more closely linked to sales volumes and are becoming increasingly flexible

After subpostmaster payments, POL's largest expenditures are: Staff Costs (**c.£231m**); IT and Operations (**c.£123m**); and Property (**c.£55m**)

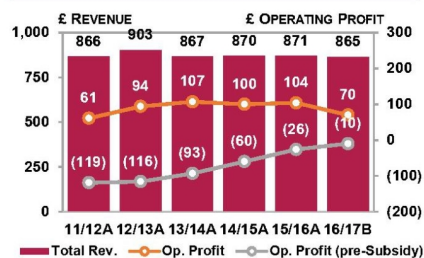
### REVENUE SPLIT (% TOTAL)

Total 2015/16A Revenue: £871m



■ Mails and Retail ■ Financial Services  
■ Government Services ■ Telephony and Other

### REVENUE & PROFIT PERFORMANCE (£m)



**LONG-TERM STRATEGY**

***POL's 2013 strategy was considered ambitious, and although the business has faced a number of challenges it has managed to meet profit targets***

***This plan was refreshed in early-2015, to keep it current in the face of difficult revenue trends***

***Management is working on a further iteration of POL's strategy at the moment, to support funding discussions that will be taking place in Autumn 2016***



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In 2013 Government agreed a new strategy with POL for the period to March 2020. It was part of the basis on which POL secured Government's recent £640m funding commitment and focuses on delivering a financially sustainable POL, less reliant on subsidy. It was centred on three core pillars

**NETWORK TRANSFORMATION**

- **Aim:** Complete the network investment strategy, modernising branches to improve customers' experience and making them less reliant on taxpayer support
- **Status:** Generally NT has progressed in line with plans

**REVENUE GROWTH**

- **Aim:** Increased sales in existing areas and launch of new products and services, focusing on particular strengths in Mails, Government Services and Financial Services
- **Status:** Slower than expected progress, with challenging demand conditions, delays to product launches and fewer new contracts than expected (particularly in Government Services)

**TRANSFORMATION AND EFFICIENCY**

- **Aim:** Reduce costs through a significant transformation of POL's IT infrastructure and a restructuring of the corporate overhead
- **Status:** Again, progress has been slower than expected, partly due to management needing to prioritise a large number different initiatives and partly due to difficult stakeholders relations

POL refreshed its 2013 plan in early 2015. While the mix of revenue and costs in this updated strategy shifted (e.g. responding to revenue trends) the overall themes, objectives and profit targets were unchanged. **POL is currently developing a further iteration of its plan which it will use to support funding discussions with Government for the period after March 2018; UKGI officials are engaging closely with POL on this**

## 6 SERVICES: MAILS AND RETAIL

*Through its exclusive relationship with Royal Mail, POL is the leading provider of retail mails services in the UK and is responsible for c.£2.5bn of Royal Mail's revenue*

*Recent years have been challenging: traditional mails products are in decline whereas key growth markets (e.g. Click and Collect) are evolving and highly competitive*

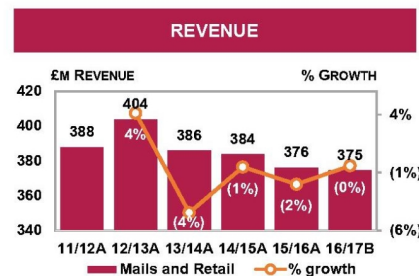
POL is the leading provider of retail mails in the UK, offering access to Royal Mail services for retail and small business customers

Range includes stamps and labels, special delivery, Parcelforce, signed-for and Home Shopping Returns; also provides selected retail services including lottery, packaging and Royal Mail / Royal Mint collectibles

A 10-year exclusive Master Distribution Agreement (MDA) was agreed with Royal Mail in 2012 on an arms length basis – this was the longest period permitted at the time by the European Commission

Royal Mail services are offered at all POL branches – this is a bigger and denser network than Royal Mail needs to meet its Universal Service Obligation

Mails is in structural decline but parcels is growing, particularly due to online retail. However competition is fierce in this segment (e.g. Collect+, MyHermes, Amazon) and the market direction is unclear



### RECENT DEVELOPMENTS / LIVE ISSUES

**ROYAL MAIL RELATIONSHIP:** Despite having a scheduled opportunity to renegotiate in 2017 POL might look to amend certain aspects of its contract with Royal Mail sooner

**COMPETITION:** The UK parcels market is increasingly fast moving and competitive. This is impacting POL as the largest provider

**MAILS STRATEGY:** POL has lacked a clear vision for its Mails business since separating from Royal Mail. It is hoped current work, that forms part of the business's broader strategy update, will address this

## 7 SERVICES: FINANCIAL SERVICES

*POL's financial services business has been transformed in recent years with the launch of a number of new services and "Post Office Money", a category focused brand for personal financial services*

*POL has also benefited in recent years from customers' perception of it as a trusted provider*

*Opportunities for future growth are strong, but not without challenges*

POL is a leading challenger in the UK Financial Services market, offering POL branded products – many in partnership with Bank of Ireland ("BoI") – and 3rd party services. POL's relationship with BoI was renewed in 2013 for 10 years

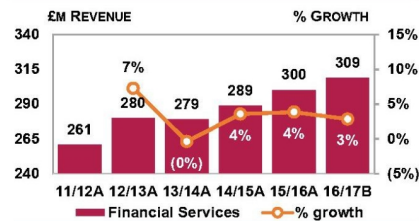
Branded products, many offered under the Post Office Money brand, cover insurance, savings, travel money, loans, mortgages, ATMs and current accounts

3<sup>rd</sup> party services include bill payments, counter services for high street banks' customers (e.g. cash withdrawal and deposit), business banking and money transfers

Recent years have seen POL focus more on its higher value branded services, e.g. launch of current accounts and mortgages, and transformation of its insurance business

This requires close strategic alignment with BoI; POL provides the retail front-end of the relationship and BoI provides balance sheet capacity, regulatory cover and support functions

### REVENUE



### RECENT DEVELOPMENTS / LIVE ISSUES

**BoI RELATIONSHIP:** POL is keen to look at changes to the BoI relationship, to bring the parties into closer alignment. This may touch on post-2023 when the current contract ends

**COUNTER SERVICES:** For the past 18 months POL has been working with banks and the BBA to develop a range of standardised services for customers of all banks. This is targeted to launch end-2016

## 8 SERVICES: GOVERNMENT SERVICES

*Revenue from Government Services has fallen in recent years, as not only have contracts been renewed on less favourable terms but expected growth in new areas has not materialised*

*POL has however won its place on a number of key frameworks*

*There could be new opportunities for POL in Identity Assurance and Assisted Digital in particular, but POL will need to ensure they can seize these opportunities*



POL is the #1 provider of over-the-counter Government Services in the UK. Its largest contracts are:

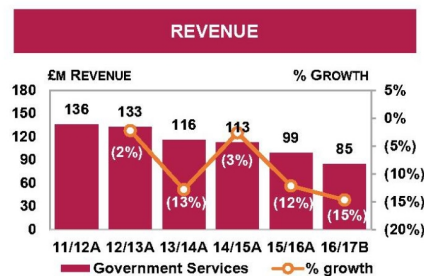
- DWP for Post Office Card Account (POCa)
- DVLA for driving license renewals and vehicle tax payment
- Home Office for Passport Check and Send

POL also provides rod licenses, Security Industry Authority verification, and visa services

Despite POL's ambition to be the "front office for Government", there have been significant challenges in recent years (i.e. competition has been intense in a number of segments, and more services have moved online). Further, it is illegal for Government to simply award contracts to POL

Key contracts have been extended but on less favourable terms, and with increased volumes migrating to direct channels (e.g. online)

New opportunities have also been slow to emerge and where they have, volumes have fallen short of expectations



### RECENT DEVELOPMENTS / LIVE ISSUES

**NEW OPPORTUNITIES / DIGITAL:** Areas where POL could play a key role (e.g. Assisted Digital, Identity Assurance) have been slower to build than expected; at the same time Digital has created pressures for POL

**FRONT OFFICE COUNTER SERVICES (FOCS):** POL is exclusive provider on this framework, enabling Departments to contract with POL easily and cheaply. Progress has been slow

**GOVERNMENT SERVICES STRATEGY:** POL has historically lacked a clear vision for Government Services. This is being addressed

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**SERVICES: TELEPHONY AND OTHER**

*The UK telecoms market is competitive and fast evolving – POL's products have particular strength among older customers who trust the brand*

*POL is responding to market developments with new product launches and a broader review of its market position*

*POL is in the process of exiting its external Supply Chain business, as it is unprofitable. This accounts for c.£[●]m revenue a year*

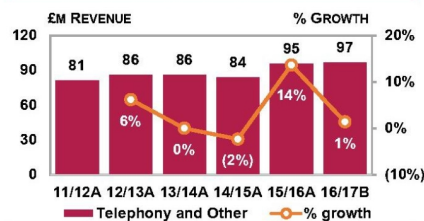


**TELEPHONY:** POL is the fifth largest provider of home phone and broadband services in the UK with c.450k customers. It focuses on value and has a particular strength among older customers. Success in recent years has been achieved through active management of pricing

POL's telephony product is provided by Fujitsu and is Post Office branded. It moved across from BT in 2013 in a challenging migration process; these were reflected in impacts on customer satisfaction and retention rates

The market is fast evolving with consolidation among telecoms firms and the line between telecoms and media fading. Traditionally POL has struggled to catch up with the market (e.g. it recently withdrew from mobile, and is expected to launch a high-speed internet product soon)

**OTHER:** POL is the #3 cash distributor in the UK, however this is not a profitable service. It will be withdrawing from this market in 2016/17 leading to redundancies and the closure of a number of depots. Separately POL also earns revenue from Royal Mail from warehousing services

**REVENUE****RECENT DEVELOPMENTS / LIVE ISSUES**

**CASH SUPPLY RESTRUCTURING:** POL is shutting its external cash supply activity in 2016/17, leading to depot closures and redundancies. This is a major contributing factor to tensions with POL's unions

**STRATEGIC REVIEW:** POL has been reviewing its strategic positioning in the telecoms market; after a number of years of lacking clarity a new plan is expected to form part of the ongoing group-wide strategy development process

**HOME SERVICES:** POL has previously looked at launching energy supply services



10 **NETWORK**

***Post Office's network stands at around 11,600 branches across the UK***

***Of this, only c.300 are owned and operated by POL; the remainder are sub post offices operated by independent businesspeople or retailers***

***POL's Network Transformation (NT) programme is making good progress at modernising the branch network, although there is still work to be done***

POL operates the largest retail network in the UK, larger than that of the four major banks combined. Funding from Government requires it to operate a network above a commercially-optimal size and meet a set of strictly-defined access criteria

The vast majority (97%) of Post Office branches are not operated by POL directly, but by a subpostmaster or a multiple retailer (e.g. WH Smith, Tesco) – these are known as sub post offices or agency branches. The contract between a subpostmaster or multiple retailer and POL is similar in nature to that of a franchisee. Often, agency branches are co-located in another retail premises, typically a shop or convenience store

**NETWORK TRANSFORMATION (NT)** is a central element of POL's strategy and sees a historic level of investment over six years to transform and modernise POL's agency branch network (of around 11,400 branches, although only 8,000 - 8,500 are in direct scope of NT<sup>(1)</sup>)

Network Transformation:

- ✓ Improves customer experience by investing in branch environments
- ✓ Improves operator performance by driving footfall and enabling more efficient branch operation
- ✓ Makes POL's cost base more flexible, allowing costs to move more closely with revenue
- ✓ Reduces POL's reliance on taxpayer support

Over 80% of branches eligible for NT have either completed their transformation or have contracted to do so. More detail on the Network and its transformation programme is provided in the annexes





## 11 BOARD AND MANAGEMENT

***POL is governed by a fiduciary Board, chaired by Tim Parker.***

***The Board is functioning well, and is now relatively stable in composition after a period of change over the last financial year***

***The CEO has been in place since POL became an independent company in 2012, and the executive team is stable, with a good CFO. Remuneration is and will continue to be a key issue regarding the quality of management***

### MANAGEMENT OVERVIEW

POL's Board consists of a Chair and five Non-Executive Directors, together with the Chief Executive Paula Vennells and Chief Financial Officer Al Cameron

The current Non-Executives are:

- Tim Parker, Chair (joined October 2015)
- Ken McCall, Senior Independent Director (joined January 2016)
- Virginia Holmes, NED (joined April 2012)
- Tim Franklin, NED (joined September 2012)
- Carla Stent, NED (joined January 2016)
- Richard Callard, NED (UKGI representative)

Overall, we consider that the Board works well. Their primarily private sector specialisms (particularly retail and financial services) drive a more commercial outlook for the company

Ministers approve remuneration for the CEO and CFO, including base pay and bonuses. Remuneration has been a sensitive issue, balancing public sector pay restraint with attracting and retaining private sector talent

### CURRENT ISSUES

With three new Board members appointed within the last year, and Tim Franklin's term as NED extended for a further three years, the Board is now relatively stable with a mixture of experience and new blood. No further changes are planned for the next 18 months

The remuneration framework for the CEO and CFO for the current financial year is currently with the CST for clearance, having been approved by Ministers in July. These arrangements relate only to base pay and short term incentive plans: POL are considering the appropriate targets for the long-term incentive plan in the light of ongoing work on their future strategy. The Remuneration Committee will submit a proposal to Ministers in the autumn



## KEY STAKEHOLDERS

*In general, stakeholders support the large scale investment in the post office network*

*The Unions are hostile to cost reduction in the core POL team – industrial action is likely especially from the CWU*

*POL has robust contingency plans in place to mitigate the expected industrial action*

### NATIONAL FEDERATION OF SUB POSTMASTERS (NFSP)

The NFSP is the body that represents subpostmasters – the independent business people who run the vast majority of Post Offices. POL has recently started funding the NFSP directly, to enable it to transform into a trade association working in partnership with POL and not a union-like organisation often in conflict with it. Although this has been widely welcomed there remain tensions in the group's relationship with POL (e.g. the NFSP negotiates with POL on subpostmaster remuneration)

In addition some subpostmasters, including certain multiple retailers who operate large batches of branches, believe the NFSP is now compromised as it received funding direct from POL. Since POL started funding the NFSP membership has been free, but take-up has fallen below expectations

### COMMUNICATIONS WORKERS UNION (CWU) & UNITE COMMUNICATION MANAGERS ASSOCIATION (CMA)

Of POL's c.6,600 staff, the CWU represent c.4,000 non-managerial grades and Unite CMA represent c.800 manager grades. Because of the scale of business reform underway (c.2,000 jobs going over the next 15 months and the defined benefit pension scheme being closed) both unions met Baroness Neville Rolfe in March to register their concerns

The CWU has since campaigned with rallies and a modestly attended "Battle Bus" national tour, and we expect it to ballot for industrial action soon. Indications from POL are that while CWU will get a good turnout for the ballot, strike turnout is likely to be low. Usefully, POL has agreed terms with Unite who are now content with terms of staff reductions; this support will help to mitigate any action the CWU might take

**We recommend you receive further briefing on this subject, and POL would be happy to meet with you to provide any further briefing or information**

## HORIZON IT SYSTEM: COMPLAINTS AND LEGAL ACTION

***There has been over two years of independent scrutiny of POL's Horizon IT system and no evidence of systemic flaws has been found***

***POL have offered mediation to those affected and in some cases have reached agreement, but others remain unresolved***

***Group civil litigation is being taken against POL by 91 claimants. This is still at an early stage. The Criminal Cases Review Commission are looking at around 20 cases***

Following complaints from a small number of (mostly former) subpostmasters about the Horizon IT system, in 2012 POL commissioned an independent firm, Second Sight, to examine the system for systemic flaws that could cause accounting discrepancies

Second Sight's interim report, published in July 2013, and final report, published in April 2015, both make clear that there is no evidence of system-wide problems with Horizon

The interim report raised some questions about the training and support offered to some subpostmasters, and POL implemented a series of measures to improve its processes. It also created a mediation scheme to consider individual subpostmasters' cases

This scheme gave applicants the opportunity to have their case reinvestigated by POL and Second Sight, and to enter a mediation process with POL to seek resolution. This scheme was independent of Government and details of individual cases are confidential. While some cases were resolved through mediation, a number were not – in particular, cases where individuals had received criminal convictions (e.g. theft or false accounting), since mediation cannot overturn a Court judgement

Earlier this year, group civil litigation on behalf of 91 claimants was commenced at the High Court. This is at an early stage and precise details of the claim are unclear. As there are legal proceedings underway, our advice is that this should remain independent of Government: it is a matter of law

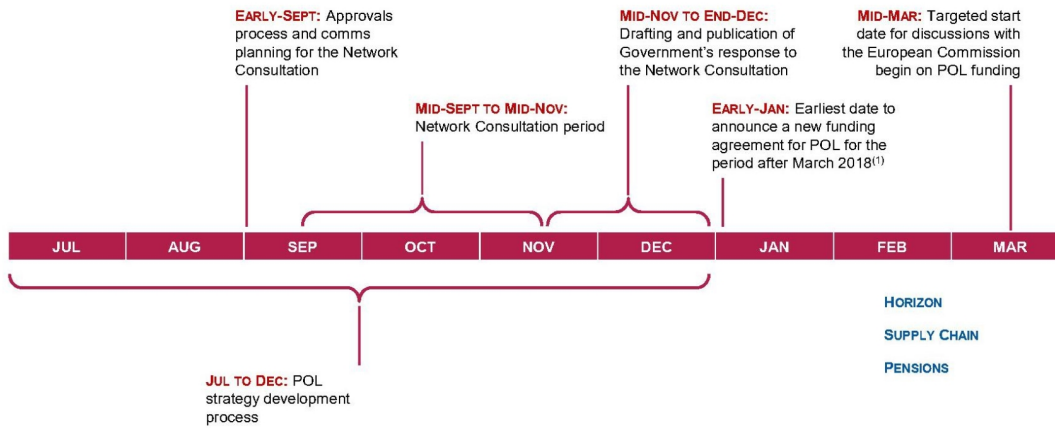
The Criminal Cases Review Commission (CCRC) is understood to be considering c.20 cases raised on this subject. This review has been underway since early 2015; we have no indication of when the CCRC may reach conclusions on any of the cases. POL are engaging fully with the CCRC's work

**We recommend you receive further briefing on this subject, and POL would be happy to meet with you to provide any further briefing or information**

RESTRICTED – POLICY & COMMERCIAL

**Tim**  
(all to contribute)

**14** **TIMELINE TO MARCH 2017 (KEY DATES)**



RESTRICTED – POLICY & COMMERCIAL

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# ANNEXES

RESTRICTED – POLICY & COMMERCIAL

DONE

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## UPCOMING SUBMISSIONS AND SUGGESTED MEETINGS

### UPCOMING SUBMISSIONS

<b>August</b>	Advice regarding upcoming strategy and funding discussions with POL
	Advice regarding upcoming consultation on the Post Office network
	Decision on POL's request to be exempt from public sector voluntary severance caps
	Advice on a rescheduled meeting with CWU
<b>September</b>	Advice on outcome of Trustees decision on whether to close the defined benefit pension.

### SUGGESTED MEETINGS

<b>August / September</b>	Introductory meeting with Paula Vennells, CEO and Tim Parker, Chairman
<b>Before Christmas</b>	Meet George Thomson, Chair of National Federation of Subpostmasters

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**POST OFFICE OPERATING MODELS**

Model Name	Number*	Overview
Crown	315	Branches owned and operated by POL, typically located in city centres. These are mostly the largest and highest volume branches in the network and offer the widest range of services. They account for only c.3% of branch numbers but represent c.16% of revenue
Main	2,857	A high-volume model designed as part of NT that offers customers an effectively complete range of post office services. A majority of these are standalone although some are co-located with a retail business. In converting from a Traditional Branch these post offices benefit from investment that refreshes branch environments and extends opening hours. Main Model Agency Branches do not receive fixed remuneration – all payments for post office services are linked to transaction volumes
Local	2,967	A lower-volume model co-located with a retail business designed as part of NT that offers customers an extensive range of post office services. In converting from a Traditional Branch these post offices benefit from investment that refreshes branch environments and extends opening hours. Co-location of the retail till also frees up space for retail use, and frees up employee time which delivers efficiency and cost-savings for subpostmasters. Local Model Agency Branches do not receive fixed remuneration – all payments for post office services are linked to transaction volumes
Traditional	2,262	Traditional post offices that are capable of converting to be a Main or Local, or which exist in a community with suitable premises that could host such a Branch (e.g. an existing post office might convert "offsite" by closing and being replaced by a Main or Local Model Agency Branch in a new location). Traditional branches are often underinvested, operate short opening hours, use "fortress" positions not aligned to modern retail markets and receive some fixed remuneration
Community	1,961	A branch that cannot convert to a Main or Local due to it being unviable as one of these models, or it is exempted from NT due to the lack of alternative hosts nearby (e.g. "last shops"). These maintain current pay structures and can access a £20 million Community Branch Fund which allows operators to invest in branches
Outreach	1,290	Post offices operating in shared premises (e.g. a community centre for a scheduled amount of time each week) or mobile from secured vehicles (e.g. with scheduled routes). Almost all of these branches are also considered to be "Community" branches and can access the £20 million Community Branch Fund
<b>Total</b>	<b>11,652</b>	

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\*Numbers correct as of end-May 2016



## 17 NETWORK TRANSFORMATION

*NT has improved the offer to customers with better layouts and hugely increased opening hours - over 200,000 extra hours every week have been added to the network since 2012*

*Changes to fixed pay have also helped reduce subsidy, from £210m in 2012 to £80m today*

*The space freed up in smaller stores and the better layouts in larger ones have helped postmasters improve non-Post Office retail by almost 10%*

NT is a combination of:

**PHYSICAL CHANGE:** Modernising and investing in branches to make them brighter and more welcoming, and extending opening hours. This includes reducing the number of “fortress” style counters in favour of open plan positions in Mains, and in Locals allowing the post office till to be co-located with the retail till (this frees up space used for the “fortress”). While many modernisations have taken place “on site” many branches have also relocated as part of NT; these usually move from being standalone branches to be co-located with retailers (e.g. convenience stores)

**CONTRACTUAL CHANGE:** Variablising remuneration structures and linking them to transaction volumes; this aligns subpostmasters interests with those of POL (i.e. subpostmasters are better incentivised to sell more effectively). The change involves removing the fixed element of subpostmaster pay worth about £10k p.a. (known as the “Core Tier Payment” or CTP)

NT has been a success with more than 6,000 branches modernised to date and POL expects to convert c.7,500 by the scheduled end of the programme in March 2018. This leaves c.500-800 “unmodernised” branches – POL is currently working on alternative solutions for these locations

Now the majority of work on NT is complete, POL is in the process of downsizing its programme team. Employee numbers are expected to fall from c.610 posts today to c.50 by next March

*Note: For further information on the different types of branches that POL operates, including the NT models (i.e. “Main” and “Local” Post Offices) see Page 18.*

## BOARD AND MANAGEMENT PROFILES

**GRO**

### Tim Parker, Chair

Tim became Chair of POL in October 2015. He has an extensive retail career and experience of business transformation, including CEO roles at Clarkes, Kwik-fit and Samsonite. He is also currently Chair of the National Trust.

**GRO**

### Ken McCall, SID

Ken took on the SID role in January 2016. A serving executive at Europcar Group, he also has a strong mails background including Chief Executive roles at DHL and TNT. Ken is also a NED at Supergroup plc.

**GRO**

### Virginia Holmes, NED

Virginia brings extensive financial services experience to the Board, including more than a decade at Barclays Bank, and a number of current Board roles. She has served on POL's Board since April 2012 and is on her second three-year term.

**GRO**

### Carla Stent, NED

Carla chairs the Audit, Risk and Compliance sub-committee, and has been in the role since January 2016. A chartered accountant, she has executive experience across banking, private equity and retail.

**GRO**

### Tim Franklin, NED

Tim's career spans both building societies and banking, including roles at Barclays and Link Cash, as well as the Land Registry. He has served on the Board since 2012 and has just renewed for a second term, to end September 2019.

**GRO**

### Richard Callard, NED

Richard is the head of the Post Office team in UK Government Investments and is the shareholder representative on the Board. A chartered accountant, he previously worked at Deloitte before joining the civil service.

**GRO**

### Paula Vennells, Chief Executive Officer

Paula became Chief Executive in 2012 having been the managing director of the network prior to that point. Her previous roles include commercial director at Whitbread plc and has worked at other major retailers including Argos and Dixons. She also has non-executive roles at Morrisons plc and Hymns Ancient and Modern Group, and is a Trustee of Go ON UK.

**GRO**

### Al Cameron, Chief Financial Officer

Appointed in January 2015, Al had a number of roles at Centrica plc, including finance director of British Gas. He was brought in for his experience of turning around businesses that required significant cost reductions in a regulated customer oriented environment. He is also a NED on the Board of Oxford University Hospitals.

## 19 REMUNERATION

Remuneration of the Executive members of the Board must be approved by the Secretary of State and the Chief Secretary to the Treasury each year. This involves approval of their base pay and bonus arrangements. The Remuneration Committee of POL (RemCo) present their proposals to the Shareholder each year to seek approval

The packages for Paula and Al are noted below, but it is worth noting that remuneration has tended to be a sensitive topic for ministers and the Board alike:

- The Board, via the RemCo, seek to motivate, attract and retain talent through offering sufficient pay packages to the executives, balanced against pay restraint required by the public sector
- Paula's base salary has not increased since she took the role in 2011, and benchmarking would suggest that her remuneration is significantly behind that of a similarly sized commercial company. Furthermore, salaries of other members of the executive team (below Board level) have increased and the gap between them and Paula has become much smaller
- Nevertheless, Paula's pay (and Al's) are high compared to public sector levels, and the shareholder team continues to try and balance these competing tensions

Details of Paula and Al's pay are as follows, reflecting the outturns for the respective years. **Note that 2015-16 figures are not yet public**

Paula Vennells	2015-16	2014-15	Al Cameron	2015-16	2014-15***
Base Pay	£250k	£250k	Base Pay	£240k	£60k
Other benefits	£72k	£71k	Other benefits	£70k	£18k
Short Term Incentive Plan*	£154k	£88k	Short Term Incentive Plan*	£125k + £75k****	£15k
Long Term Incentive Plan**	£144k	£112k	Long Term Incentive Plan**	n/a	n/a
<b>Total for year</b>	<b>£619k</b>	<b>£521k</b>	<b>Total for year</b>	<b>£509k</b>	<b>£93k</b>

\* Targets for the STIP are based on metrics such as revenues, profits, customer satisfaction, network transformation etc.

\*\* The LTIP target is based on maintaining a minimum level of branches and achieving profit targets

\*\*\* Al joined POL in January 2015, so the figures given relate only to part of the year. There was no change to base pay or bonus structure between financial years.

\*\*\*\* The £75,000 relates to a one-off bonus payable after 6 months in post against agreed objectives, to compensate for salary/bonus reductions on joining POL

## 20 Legal Structure

POL is 100% owned by Government, via a holding company that also previously owned Government's shareholding in Royal Mail

Now the remaining shares in Royal Mail have been sold, there are plans to wind-down POSH to simplify POL's shareholding structure

POL is subject to Companies Act provisions, competition law, and European framework (i.e. State Aid)



### OVERVIEW

POL separated from Royal Mail in 2012 prior to the sale of Royal Mail shares. It is now 100% directly owned by Government through POSH

- Set up to hold Government's stake in Royal Mail and its shareholding in POL
- POSH Board is made up of 3 directors (2x UKGI and 1x Other BEIS)

Through POSH Government holds a special share in POL

- Gives a range of rights including approving appointment of directors and directors' remuneration
- Other rights relate to matters such as sale of assets, changes to strategy, changes to governance structures, etc.

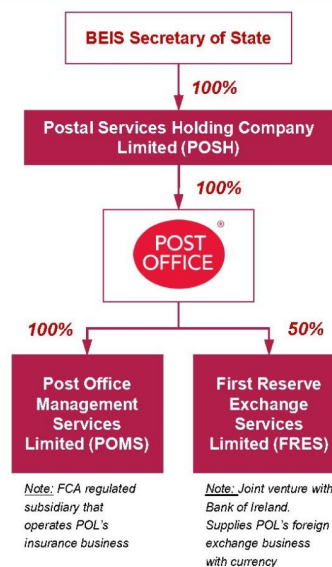
POL's regulated insurance business is run through a subsidiary called POMS

- Restructured in 2015 to allow POL to transform its insurance activities

POL also owns a 50% stake in FRES

- Joint venture with Bank of Ireland, supplying POL's bureau de change business with currency

### STRUCTURE



21 Recent Developments / Live Issues – Mails and Retail

Royal Mail Relationship	Competition	Mails Strategy
<ul style="list-style-type: none"> <li>POL's contract with RM was signed in 2012 before the separation of the two businesses. It is a commercial agreement agreed on an arms-length basis and, with a 10-year duration, was the longest permitted by the European Commission at the time.</li> <li>Government was not involved in the discussions and has also not sought to influence this relationship. Any such action would have significant legal and financial implications for POL and RM.</li> <li>The contract has a "renegotiation event" scheduled for 2017 when the contract can be revised, but POL is considering opening discussions with RM sooner. Formal dialogue may commence during 2015.</li> <li>POL is keen to realign certain aspects of the relationship as in recent months tensions have emerged (e.g. around POL's plans to grow its network and in relation to product structuring, pricing and new launches (e.g. Click and Collect)).</li> </ul>	<ul style="list-style-type: none"> <li>With the letters market in structural decline POL and RM see the opportunity in parcels as the biggest source of retail Mails growth. However in recent years a number of competitors have emerged, placing pressures on both parties</li> <li>Many grocery stores now work with competing parcel delivery providers (e.g. Collect+, MyHermes) while other areas of the market are innovating fast (e.g. Amazon Logistics, retailers' Click and Collect, same-day delivery, etc.). There are now more pick-up/drop-off points for parcels (i.e. rival services) than there are Post Office branches</li> <li>The impact of increased competition is being compounded by the fact that expected growth in the parcels market has not materialised. It is also not clear whether POL and RM are offering the right product set (e.g. simplicity and price)</li> </ul>	<ul style="list-style-type: none"> <li>Historically POL has not taken a strategic approach to its Mails business, instead seeing itself as a supplier to RM</li> <li>This has negatively impacted POL in recent years as RM's strategy has been exposed to unexpected changes in the market. In response POL is now taking action to develop its own Mails plan</li> <li>The early work coming out of POL's strengthened Mails team is encouraging and the outputs of this work are expected to feed into POL's broader strategic refresh which will be presented to Government in mid-2015</li> <li>This is focused on optimising POL's position in the market and it could look at some radical options (e.g. looking at ways POL could move away from its exclusive relationship with RM in some segments of the market)</li> </ul>

## Recent Developments / Live Issues – Financial Services

### Bank of Ireland (BoI) Relationship

- The majority of POL's own-branded financial services are provided in conjunction with BoI. POL provides exclusive access to its retail network and customers, while BoI brings balance sheet capacity and product / technical support. The relationship has historically worked well and financial services has been a key growth area for POL.
- In recent months tensions have emerged (e.g. in respect of current accounts, mortgages and savings and investments) and discussions to address these issues are ongoing. It is important that progress can be made so that POL can deliver planned income growth (e.g. new product launches) and meet its financial targets.
- POL expects BoI will want some clarity for the period after 2023 when the current contract ends and are considering handling.

### Counter Services

- Today 98% personal current account customers and a large number of SMEs can make withdrawals and deposits at post offices and check their balances, albeit not in a consistent manner (e.g. the way to deposit differs between banks). Most recently, Santander agreed to make this service available to its current account customers.
- Since December 2014 POL has been working with the high-street banks and the BBA to launch a standardised offer that would make a consistent service available to all personal and SME customers. The challenge for POL will be to ensure the agreement works for them commercially.
- After a good start progress has slowed recently. Despite this POL remains hopeful of successfully taking the opportunity forward, in particular as it would be a welcome revenue upside for the business.



## Recent Developments / Live Issues – Govt. Services

### New Opportunities / Digital

- POL has faced considerable disappointment in its efforts to grow Government Services in recent years as significant revenue opportunities have been deferred or have failed to materialise, and as such, POL exercise a degree of caution in respect of the opportunities below.
- **Passport Applications:** POL is working with the Home Office on the possible launch of a POL digital passport applications service, with potential launch in November 2015 to coincide with HMPO's digital journey public beta.
- **Assisted Digital:** POL is an obvious candidate to provide AD services (for those who can't or won't use digital channels), but POL will need to be certain on future volumes and revenues to invest in both kit and training
- **Identity Assurance:** POL launched its IdA product on the Government Verify service in pilot phase in April and is currently gaining around 60% of that market. Progress has been slow to date but volumes are now well above expectations – the challenge will be to sustain this and innovate further.

### Front Office Counter Services (FOCS)

- In 2012 POL won a tender for the FOCS contract, which is an exclusive framework enabling Departments to contract with POL without running separate time consuming and costly procurements. Contracts under FOCS have a duration of 7-years, with the option for a 2 year extension. This means that call-offs from FOCS can be made at any time during the life of the underlying contract for 7 years (plus the extension).
- FOCS was expected to unlock a number of new Government Services opportunities but since 2012 only existing contracts have moved to this framework (e.g. DVLA, POca and Passport Check and Send).
- Few new opportunities have emerged despite considerable work to improve Whitehall's knowledge and understanding of this opportunity, and to find ways to align the interests of FOCS with the Government Digital Service.

### Government Services Strategy

- Over recent years the Digital by Default agenda has been implemented across Whitehall, reflecting a growing preference by the public to interact with Government online, and as a means to reduce admin costs.
- Led by the Government Digital Service (GDS), key Government services and transactions have moved online and been adapted for the digital journey.
- However, the Digital by Default agenda conflicts directly with the ambition to make Post Office a front office for Government. Departments hosting online services have to consider the value for money case for offering non-digital offerings (e.g. post, phone, or counter services). With volumes both uncertain and diminishing, Government Services contracts are less profitable and appealing for POL.
- There have been instances where GDS has appeared to block Departments taking forward services with POL, although there are some new opportunities too (see right).



**Recent Developments / Live Issues – Telephony / Other****Cash Supply Restructuring**

- POL's supply chain activity is high cost, highly unionised and lacks the innovation of its peers.
- While POL is taking some actions to reduce costs (e.g. redundancies, new vehicles, etc.) it is also looking at ways in which it can reposition the business (e.g. simplifying products, changing the way branches demand and manage cash).
- Changes must be managed carefully. Anything that risks branches' access to cash has significant reputational and operational implications (e.g. for POL and Government, and for vulnerable customers unable to access benefits).

**Strategic Review**

- In response to significant recent changes in the UK telecoms market, in the last few months POL has initiated a review of its telephony business.
- POL needs a clear long-term strategy and business case to justify investment in mobile and high-speed internet, and it also needs a plan on how it can win customers in an intensely competitive environment.
- One option POL has considered, on a very preliminary basis, is a sale of its customer base or a combination of its telephony business with one of its peers.
- It is important to note that shareholder approval will be required before any process can formally commence and before any transaction can take place.

**Home Services**

- When POL developed its overall strategy in 2013 it proposed setting up a Home Services business, starting with the launch of a POL branded energy supply activity.
- Given the reputational damage experienced by many energy suppliers in recent years it was thought that this would be an attractive opportunity for POL (e.g. the right product would be aligned to POL's trusted brand).
- However given POL's focus on delivering the core of its strategy and due to changes in the regulatory and competitive environment that make a launch more complex, POL has currently put this on-hold.
- While it remains a possible area for future expansion, POL is not expected to take action in the near-term.

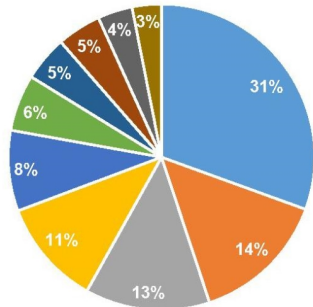
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25 **Business Overview – Revenue Split**

**MAILS AND RETAIL (£m)**

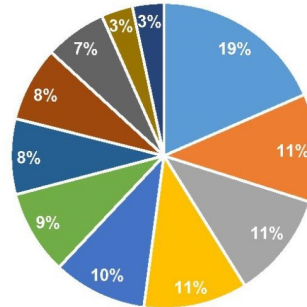
Total 2015/16 Revenue: £376m



- Stamps and Labels
- Fixed Fee
- Special Delivery
- Retail and Lottery
- Int'l Priority and Standard
- Signed For
- Parcelforce
- Other Mails
- Mailwork and Mails Non-trading
- Home Shopping Returns

**FINANCIAL SERVICES (£m)**

Total 2015/16 Revenue: £300m



- Savings
- ATM
- Insurance
- Personal Banking Clients
- Bill Payment
- MoneyGram
- Business Banking
- Bureau and Travel Money Card
- Postal Orders
- Lending
- Other

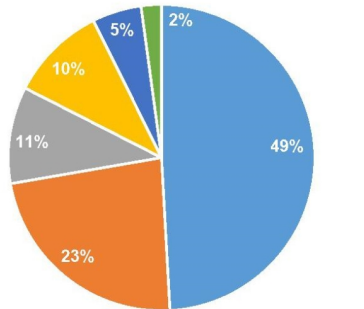
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26 **Business Overview – Revenue Split (cont.)**

**GOVERNMENT SERVICES (£m)**

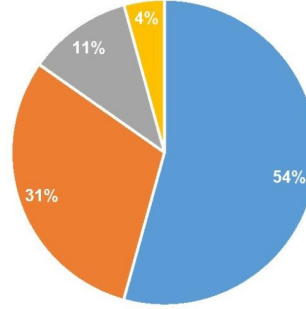
Total 2015/16 Revenue: £99m



- POca
- Passport Services
- Motoring Services
- Digital ID Services, UKVI and Asylum
- Other Government Services
- IS Assurance

**TELEPHONY AND OTHER (£m)**

Total 2015/16 Revenue: £95m



- HomePhone and Broadband
- Supply Chain
- Other Income
- Other Telephony and Mobile