

[Post Office Limited Letterhead]

[Chairman of the Working Group]

[] 2014

Dear [Sir]

Initial Complaint Review and Mediation Scheme

As you know, Post Office Limited (the “**Post Office**”) set up the Initial Complaint Review and Mediation Scheme (“**the Scheme**”) to seek to provide a mechanism for resolving complaints which certain Sub-Postmasters (“**SPMRs**”) had about the operation of the Horizon transaction reporting system. Much work has now been done in the context of the Scheme and the Post Office has carefully considered the information so far available as to the operation of Horizon, the nature of the individual complaints brought and the Post Office's preliminary response to the issues raised in those complaints.

The result of the Post Office's own work in relation to the Scheme is that the Post Office now has certain views on issues which arise in many, if not all, complaints, and the Post Office believes that it would be appropriate to share those with the Working Group through this letter. I shall also be arranging for a copy of this letter to be posted on the [website] so that all those interested can read it. I should stress that each complaint is and will be addressed individually and on its own merits. Nothing in this letter should be taken as leading to a firm conclusion in relation to the merits of any individual complaint. Nevertheless, to the extent to which this letter sets out the Post Office's thinking in relation to a particular point, the likelihood is that there would need to be specific facts in an individual complaint to lead the Post Office to form a different conclusion on that issue.

The Post Office would be happy to explain its thinking on any of these issues further or to clarify any point where you, as Chairman of the Working Group, thought that that would be of assistance.

The Post Office recognises that certain SPMRs have been frustrated and upset about their dealings with the Horizon system (though I note that it is only a very small minority of SPMRs who describe their experience with Horizon in these terms). The Post Office is and remains concerned about any and all such reactions and wishes to work with SPMRs both to understand their complaints and also to ensure, so far as possible, that individual SPMRs are able to work with Horizon to ensure a problem-free relationship in the future. Where a SPMR has translated his or her reactions to Horizon into a complaint it is inevitable that the analysis will turn on the legal framework between the SPMRs and the Post Office and the question of whether such a complaint is made out will be one answered by reference to legal principles. The Post Office is bound to consider complaints in this way, not least because it has a number of stakeholders to whom it is answerable and has also to bear in mind the interests of other users of Horizon from whom the Post Office may have claimed losses but who have not complained. The Post Office believes that the right course is for it only to consider paying compensation to SPMRs where that is the correct conclusion as a matter of the law.

[We should try to say something about the entrance requirements into the Scheme. The SPMRs will ask why they are in the Scheme if they don't have claims.]

For the reasons set out more fully in this letter, the Post Office considers that many, if not most, of the complaints in the Scheme lack or are likely to lack a reasonable legal basis. The Post Office is keen to moderate the expectations of SPMRs who have brought complaints and hopes that this letter may assist in that process.

Against that background, the issues addressed in this letter are as follows:

- (a) The proper functioning of the Horizon system;
- (b) The contractual relationship between the Post Office and SPMRs;
- (c) The legal framework for the recovery of losses by the Post Office;
- (d) The Post Office's obligations in relation to training and support;
- (e) The right of the Post Office to terminate a contract with a SPMR;
- (f) The legal right of SPMRs to compensation; and
- (g) The application of the Limitation Act 1980.

The proper functioning of the Horizon system

The complaints in the Scheme, necessarily, are about or are associated with Horizon. They are not about other aspects of the Post Office/ SPMR relationship. The Post Office's liability to any particular applicant, therefore, depends in large measure on there being, generally or in any particular case, a flaw in Horizon.

The Post Office notes Second Sight's preliminary conclusion, that they "found no evidence of system wide (systemic) problems with the Horizon software." [The Post Office has, of course, read what Second Sight has produced and taken it into account. However, it is concerned that the work of Second Sight does not address the operation of Horizon in comprehensive terms. The Post Office is also concerned about the level of detail in Second Sight's work and the lack of evident substantiation for Second Sight's views.]

By way of supplement to Second Sight's work, therefore, the Post Office has commissioned a report from Deloitte (the "**Deloitte Report**"). The Deloitte Report [confirms what the Post Office [believes/has been confident] has always been the case: Horizon is fit for purpose and functions in accordance with its design specifications; it is not fundamentally flawed; it does not suffer from any systemic issues. In particular, the Deloitte report:

[Set out key findings of the Deloitte Report]

[A copy of the Deloitte Report is enclosed./ The Post Office has distributed /will be distributing [in due course] copies of the Deloitte Report to you and to other relevant interested parties.]

The Post Office believes that the conclusions Deloitte have reached about Horizon removes any doubts over its functionality or its fitness for purpose.

The Post Office will, of course, consider carefully specific allegations made in a particular case. But in doing so the Post Office will be guided by what Deloitte's view is as to the likelihood of the particular issue impacting on the performance of Horizon. ***[This needs further thought as to how the Post Office wishes to position it. Moreover, what does the Post Office want to say about Second Sight?]***

The contractual relationship between the Post Office and SPMRs

The legal relationship between SPMRs and the Post Office is governed by the 1994 standard form contract (the “**Contract**”). It is important to recognise that the Contract (together with the general law) provides the framework for the allocation of risk between the Post Office and SPMRs. That framework must guide the determination of any liability owed, in either direction, between applicants to the Scheme and the Post Office.

The legal framework for the recovery of losses by the Post Office

Clause 1 of the Contract makes it clear that the relationship is one of principal and agent and that the SPMRs are not employees of the Post Office. The Contract, and agency relationship, have several key consequences. First, they give rise to certain, clear duties owed by SPMRs to the Post Office (which I mention further below). Secondly, SPMRs do not enjoy the legal protections and benefits that they otherwise might if they had the status of employees (see, for example, *Commissioners of Inland Revenue v Post Office Limited* [2003] ICR 546 and *Moeze Lalji v Post Office Limited* [2007] EWHC 5 (QB)). Thirdly, such duties as the Post Office might owe SPMRs are established and circumscribed by the terms of the Contract i.e. there can be no broader duty of care which would extend the contractual duties owed by the Post Office in any respect relevant to the subject matter of complaints in the Scheme.

There are two main issues in the recovery of losses: 1) the way in which losses are calculated and 2) the Post Office's legal entitlement to seek those losses from a SPMR. It is accepted by all that Horizon produces and maintains the accounts on which all parties rely. The Post Office's position is that, as a matter of principle, Horizon accurately reflects the account between the Post Office (i.e. it accurately calculates losses) and that the Post Office is entitled to recover such losses from SPMRs, including the applicants to the Scheme.

The SPMR is, day to day, responsible for inputting transactions to the Horizon system. Horizon provides a record not only of what the SPMR has received from the Post Office by way of stock but also what he has sold, and the cash he has received. Horizon is the only system used to record transactions; the Post Office holds no other relevant records. During the period covered by the complaints to the Scheme, at least once a month and potentially as often as at the end of every week, a SPMR was obliged to prepare and sign a document entitled “Cash Account (Final)” and send it to the Post Office or complete an equivalent process by declaring via an electronic system the amount of cash that he holds. The SPMR also conducted a manual hand count of cash and stock in the branch and compared them to the levels recorded in Horizon.

Section 12, paragraph 4 of the Contract provides:

“The Subpostmaster must ensure that accounts of all stock and cash entrusted to him by Post Office Ltd are kept in the form prescribed by Post Office Ltd. He must immediately produce these accounts, and the whole of his Post Office branch cash and stock for inspection whenever so requested by a person duly authorised by Post Office Ltd.”

Therefore, there is a clear contractual basis on which SPMRs are required to account to the Post Office whenever requested to do so. In any event, the duty to keep an account also arises under the general law by virtue of the principal/agent relationship. An agent is required to keep an accurate account of all transactions entered into within the scope of his agency and he has to be ready to produce that account at any time to his principal. If he fails to keep and produce accounts then the principal is entitled to assume everything against him. SPMRs are asked to agree accounts regularly. They signify their agreement by an appropriate entry on Horizon. If a SPMR disputes the state of his account, he is free not to agree that account on Horizon.

An agent is bound by his own accounts unless he can show that he made a mistake. Once an account is agreed, the principal can sue on it. In other words, once a SPMR signifies his agreement to an account on Horizon which shows a balance due to the Post Office, the Post Office is entitled to sue on this as an account stated (see, for example, *Post Office Limited v Lee Castleton* [2007] EWHC 5 (QB)). Generally, settled accounts will not be re-opened, unless (as mentioned) drawn up under a mistake or if the agent is guilty of fraud.

Thus, as I mention above, it is the reliability of the Horizon system as a matter of principle which is important because its reliability places the burden on the SPMR to show why, on the basis of the limited exceptions above, the amounts said to be owing are not in fact owed. But, there can now be no real doubt as to its reliability. The circumstances, therefore, in which any applicant to the Scheme could realistically “re-open an account” and object to a particular loss recovery will be limited indeed.

The complaints to the Scheme do not appear to take issue with the Post Office's right, as a matter of principle, to recover losses from SPMRs. However, there can be no doubt that such a right exists. First, section 12, paragraph 12 of the Contract is headed Losses. It provides:

“The Subpostmaster is responsible for all losses caused through his own negligence, carelessness or error, and also for losses of all kinds caused by his Assistants. Deficiencies due to such losses must be made good without delay.”

Paragraph 13 makes it clear that this obligation does not cease on the SPMR relinquishing his appointment and extends to losses which come to light after he leaves. Further, the fact that the SPMR must be in “error” is a low threshold and implies the Post Office need not establish any “mental element” on the part of the SPMR: he can simply be mistaken without being careless and without there being any question of dishonesty on his part.

Absent the right contained in section 12, paragraph 12, the Post Office would in any event be entitled under the general law to seek loss recovery pursuant to the duty of an agent who holds money for his principal to pay over or account for that money at the request of his principal. Thus there is a sound contractual basis for the recovery of losses, which is supported and supplemented by the general law governing an agent's duties to his principal.

The Post Office's obligations in relation to training and support

The Post Office is obliged to provide training under section 15, paragraph 7 of the Contract. In particular, the Post Office agrees to provide the Subpostmaster with relevant training materials and processes to carry out the required training of his Assistants on the Post Office Products and Services, inform the SPMR as soon as possible where new or revised training will be necessary as a result of changes in either the law or Post Office Services and (as necessary) update such training and materials.

However, it is the SPMR's responsibility to ensure the proper deployment within his Post Office branch of any material and processes provided by the Post Office and to ensure that his Assistants receive all the training which is necessary in order to be able properly to provide the Post Office Products and Services.

In other words, the Post Office must provide training and keep it up to date but the SPMR is still responsible for the day to day operation of the Subpostoffice and accepts the consequences of any lack of training provided to his Assistants or their failure to put the training into effect.

In any event, in order to show that a claimed failure to provide proper training or support gave rise to a complaint, the SPMR would have to show how any alleged inadequate training or support has caused the loss he claims. The Post Office believes that this will be difficult to do in most if not all cases.

The right of the Post Office to terminate a contract with a SPMR

Some complaints concern the alleged wrongful termination of Contracts. The Post Office is entitled to give three months' notice to terminate the Contract with the SPMR (under section 1, paragraph 10) for any reason. If in a particular case the SPMR's Contract has been terminated on three months' notice, he can have no remedy arising out of that termination. The Post Office is able, contractually, to terminate the Contract for any reason or, indeed, for no reason.

Section 1, paragraph 10 also entitles the Post Office to terminate a Contract with a SPMR summarily for breach of a condition or non-performance of an obligation by the SPMR. Such cases must be treated on their facts. The Post Office believes that it is likely that in most or all cases, any such loss flowing from the wrongful summary termination of a Contract would be limited to the loss of the SPMR's entitlements during the three months following the termination, because the Post Office would have otherwise been entitled to terminate the Contract (for any reason) on giving such notice. The same comments above as to causation of loss also apply.

The legal right of SPMRs to claim compensation

As a matter of principle, if in each particular case, the Post Office has a right to recover losses, then there can be no question of the relevant applicant being entitled to "compensation"; in short, there is nothing for which compensation is due. Even if the Post Office was not in a particular case entitled to claim losses (and as I say above, such cases, if any, are likely to be very limited), then it may be that the applicant has a right to recover only *the specific amount of losses* that he paid to the Post Office. This is a restitutionary, not a compensatory, claim. It does not entitle the applicant to supposed related or consequential other amounts, such as for lost earnings, distress, hurt feelings etc.

In particular, in cases where the courts have determined criminal or civil liability against an applicant in respect of loss recovery that forms the subject of the complaint, there can be no doubt whatsoever that the Post Office was entitled to the losses. There can also, for that reason, be no doubt that the Post Office is not liable to pay restitution to such applicants for any alleged wrongful loss recovery.

Cases which a court has not been asked to decide (the majority) seem to fall roughly into general allegations as to the unreliability of Horizon and specific allegations as to factors which may have affected Horizon in the particular case. Particularly in light of the Deloitte Report, general, largely unsubstantiated allegations about Horizon would not establish that a particular loss recovery exercise was wrongful and therefore that restitution to the applicant is due.

More specific allegations about the functionality of Horizon need to be looked at on a case by case basis. [The Post Office accepts that in some, albeit limited, cases there may be specific reasons why loss recovery should not have occurred. These will need to be fully investigated and dealt with.]

However, a couple of important points should be recognised here. First, the Post Office can only be liable to pay restitution for wrongful loss recovery for which it is legally responsible i.e. for things which it has caused. For example, some complaints refer to such things as power cuts, incompatible use of other technologies with Horizon, intermittent internet connectivity etc. as being the basis for the complaint. Others claim compensation where there is a real question over whether Horizon or any of the matters of which complaint is being made caused the "loss" at all. It would be very difficult in such cases to establish liability on the part of the Post Office to pay restitution (or compensation).

Secondly, as I say, the basis for any claim for wrongful loss recovery is restitutionary - i.e. the recoupment of the specific amounts originally paid by the applicant. Even to the extent an applicant could show that the loss recovery was, somehow, a breach of the Contract by the Post Office – thus entitling him to

compensation - this would only entitle the applicant to damages for losses that were reasonably in the contemplation of the parties. This would not include such consequential "losses" as loss of reputation, hurt feelings, mental distress or ill health etc. (even if such matters could be shown to have been caused by the wrongful loss recovery, itself a difficult prospect), as several complaints seem to claim.

I trust that this letter clearly conveys the Post Office's overall position in respect of the issues raised by complaints made to the Scheme. I would welcome any comments or questions you may have in response to it.

Yours sincerely