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26 October 2020 HMT Note on POL Compensation

Purpose

This note has been produced by UKGI and BEIS in preparation for the 26 October meeting with HMT regarding Post Office Ltd. (POL) compensation claims and providing public funding.

Alongside this note officials are in the process of drafting a note for ~~the CST~~ HMT ahead of Supplementary Estimates to request FY20/21 AME budget cover for BEIS.

Commented [CA-U1]: Can we make clear this is a note to help inform how we approach the business case etc. and that this note doesn't have ministerial/AO cover – it's to provide background so that HMT can help us have a successful Supps

Executive Summary

1. It has now become apparent that there are several risks starting to crystallise for POL as a result of the fallout of the Group Litigation Order (GLO) that was settled in December 2019. In simple terms, these risks boil down to POL not being able to fund various compensation claims brought against it by postmasters having i) already spent c. £120m on litigation costs to date from its own commercial revenue and ii) having its profitability significantly impacted by the pandemic. These risks are as follows:

    a. **The Historical Shortfalls Scheme (HSS):** [redacted]

    ~~a.~~

    b. **Dealing with Counterparties:** Due to the above being now unaffordable, in November/December POL will require an accounting provision, resulting in POL entering into net liabilities and defaulting on a key funding agreement it has with NatWest and cross-defaulting on its other funding agreements (including the Working Capital Facility it has with BEIS) – this could result in £100m's of key funding being withdrawn and POL becoming technically insolvent. BEIS might have to ~~backstop or~~ replace this funding at short notice. A further risk is that POL decides that HMG is in fact unwilling to stand behind the company and takes steps to protect its position, including by stopping spending on normal operations;

    ~~b.~~

    c. **Overturned Conviction Claims:** Following POL's response to the appeal courts on 2 October (where POL stated it will not oppose 44/47 cases of convicted postmasters) it is now very likely that the majority of these will be overturned. [redacted]

    d. **19/20 Accounts:** POL must file its 19/20 accounts by March 2021 as a going concern, meaning it has the ability to meet its obligations for at least the next 12 months. Without going concern status, POL's accounts may need to be 'qualified', which would result in a lack of confidence in POL's solvency from its commercial partners and attract widespread parliamentary and press attention.

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2. With POL's cash revenues now exhausted and profitability still below previous levels due to the pandemic, it will no longer be able to meet it's obligations under any of the above without diverting significant funding away from other areas of the business and impacting it's operations and policy responsibilities. Even then, it is likely that POL would still become insolvent.

3. For policy reasons, we are assuming Government won't allow POL to become insolvent, so we are working with the company to provide funding via business cases. However, in the short-term there is the issue regarding the HSS which will need resolving.

Historical Shortfall Scheme

4. Having closed for applications in August, the HSS is now materially oversubscribed and unaffordable for POL. [redacted]

5. Claims are assessed by an Independent Panel however due to the volume received it won't be until November/December that the panel will be in a position to recommend HSS claim payments to the POL Board. This is a point at which the HSS liability will be known and POL will therefore need to make a provision in its accounts, entering into net liabilities (activating risk (b)).

6. [redacted]

7. In the medium-term, POL will be submitting a business case after the Independent Panel has opined on the claims in December to request funding.

Comfort Letter

8. To reassure POL and its counterparties that BEIS would not allow POL to go insolvent and cease trading, we have drafted a comfort letter that can be seen at **Annex A**. This is still to be cleared by the BEIS Perm Sec and a draft has been shared with the company.

9. A comfort letter is not a commitment to provide any future funding, which will be subject to business cases, but as an interim measure familiar to POL and it's counterparties to satisfy i) POL's counterparties that it can continue trading, ii) POL's Directors that it can begin HSS payments without committing wrongful trading and iii) POL's auditors that POL can meet its obligations and can sign its 2019/20 accounts as a going concern.

10. This comfort letter will require approval from HMT ~~the CST~~ before being issued.

Compensation Claims Arising from Overturned Convictions

11. On 2 October, POL responded to the appeals courts stating it won't oppose the 44 of the initial 47 cases referred for appeal. It is likely the majority of these will be overturned and

Commented [WR-U2]: Not sure this is right. The panel might make some recommendations by then but not for all applicants. I think POL are hoping by early Dec their legal team will be able to give a better estimate of what the overall liability might be under the HSS but I don't think this will be a panel recommendation.

Commented [CA-U3]: Aren't we going in for Supps?

Commented [WR-U4]: See previous comment

Commented [SJ-U5]: Attach?

Commented [SJ-U6]: TBC.

Commented [CA-U7]: Let's not tie ourselves into that – hopefully Rebecca can approve it. Just say HMT

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open the door to further civil claims which in all likelihood will be [redacted]

12. [redacted]

13. It is difficult at present to land on more accurate cost estimates as POL's financial exposure relies on two keys factors out of its control; firstly, the number of claims being brought and secondly, the rulings of the appeal courts, the majority of which will not be until early next year. We expect costs to start crystallising in FY2021/22.

14. POL is exploring options to deal with further civil claims. This ranges from setting up different types of schemes, mediating with individual postmasters as claims come forward or purely reacting ~~purely~~ to further litigation. An outline of these options and their estimated costs can be seen at **Annex B**. It is the company's and BEIS' desire to avoid further litigation (which would do significant reputational damage to HMG/POL and drive costs up for all parties) and demonstrate to postmasters that POL is doing all it can to bring the Horizon ordeal to finality.

15. Regardless of whether HMG intervenes or not, these liabilities will remain with POL and will not dissipate. Issues regarding Horizon and compensating postmasters will also continue to attract significant parliamentary and media attention, particularly as more postmasters are found to have been wrongly convicted.

16. Claims arising from postmasters whose convictions are overturned are noted in the comfort letter, but again no funding has been confirmed and is subject to business case approval.

17. There is the immediate question of budget cover for BEIS at Supplementary Estimates should BEIS be required to record a provision and seek FY20/21 AME budget cover. A note is being prepared for HMT ~~the CST~~ ahead of this.

18. Once more detail is gleaned from the appeal courts, POL has committed to bring a business case for a compensation scheme to BEIS/HMT for approval in Spring 2021.

Commented [SJ-U8]: Vanisha should we say more here?

Commented [CA-U9R9]: This needs more, we need to warm them up to the size of the cover request and probably going to want them to opine on whether we should be putting in best estimate, worst case, or some other figure?

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Annex B – POL Options for Compensating Postmasters with an overturned criminal conviction

- [redacted]

[redacted]

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