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# POST OFFICE LIMITED
# GROUP EXECUTIVE REPORT

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| **Title:** | Postmaster Operational Excellence Incentives | **Meeting Date:** | 17 January 2024 |
| **Author:** | Martin Edwards, Network Strategy & Delivery Director | **Sponsor:** | Martin Roberts, Group Chief Retail Officer |

**Input Sought:** GE discussion on scheme design, value & timing

Operational Excellence Incentives (OEIs) are a proposed new component of the remuneration system designed to reward branch compliance with back office activities which help reduce discrepancies and other costs for POL. We trailed our intention to launch OEIs at the November Postmaster conference, committing to share further details as part of the annual remuneration announcements in March.

## Questions addressed

1. What is the proposed design of OEIs?
2. What are the key dependencies for successful launch of the scheme?
3. What are the expected payments and financial implications?
4. When do we propose to announce and launch the new scheme?
5. What other remuneration changes do we expect to announce in March?

## Report

### What is the proposed design of OEIs?

1. The rationale for the OEIs scheme is threefold:
   a. it should create a **win-win cycle of improved profitability for both sides**, exemplifying a partnership approach where remuneration improvements are partly funded by reductions in Post Office costs arising from branch conformance;
   b. it **demonstrates we are listening to postmaster and NFSP feedback**, addressing the perception that branches are being asked to undertake a growing workload of back office activities without direct remuneration; and
   c. the OEIs are **well targeted from a network strategy perspective**, with more money going to the more commercial branches we need to retain.
2. From a long list of over a dozen potential metrics, we have selected four lead measures for the scheme which: a) are consistent with existing operational requirements for branches; b) have a strong correlation with cost reductions for Post Office; and c) can be robustly measured and reported:
   - Trading Period Balance
   - Cash Declarations
   - Cash Pouch Errors
   - Excess Cash

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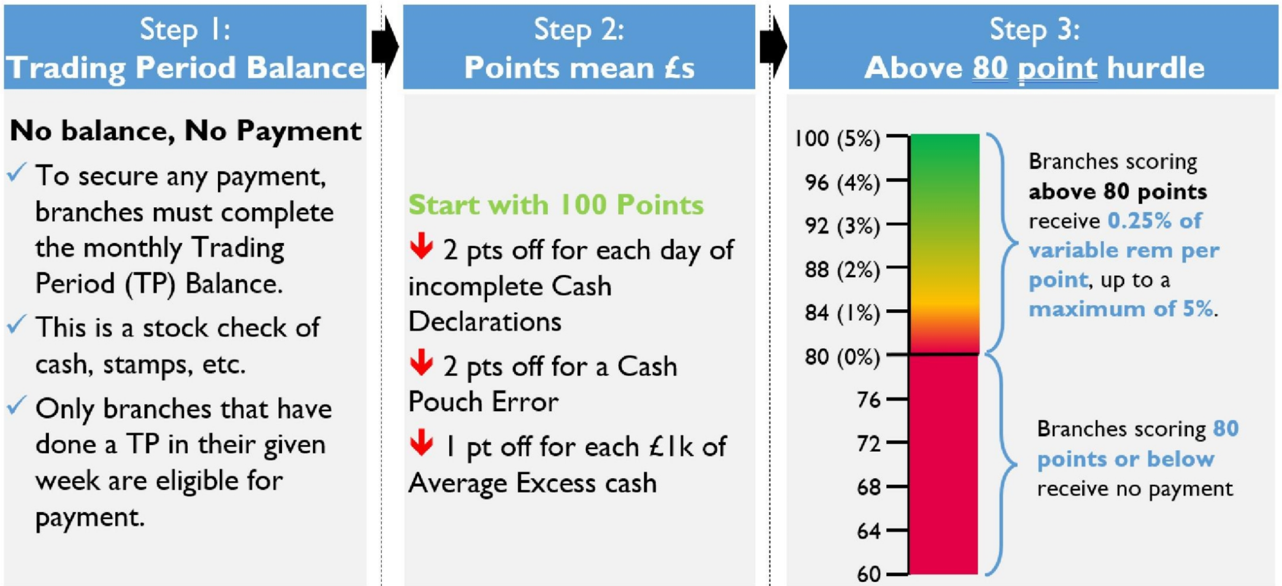
3. These activities will be measured on a monthly basis with the opportunity for branches to earn up to a 5% boost to their monthly variable remuneration, based on the scoring scheme set out in the following diagram:




4. These measures have been through multiple iterations following extensive engagement with both internal and external stakeholders, including the NFSP, five regional Postmaster Forums, two of our strategic partners (Morrisons and Hendersons), the Postmaster NEDs and the Postmaster Experience Director. Overall the feedback has been very positive, subject to us fulfilling the key dependencies set out in the next section.

## What are the key dependencies for successful launch of the scheme?

5. This engagement has reinforced the importance of two critical enablers to support the successful launch of the scheme:

   a. **Access to robust and timely data** for each branch on the performance metrics which drive the monthly incentives (as detailed above), ensuring there is complete transparency on the basis for their payments. This will be made available through a new dashboard on Branch Hub, the development of which is due to be completed by April.

   b. **A comprehensive programme of training and support** to ensure every branch is clear on the correct processes they need to follow to receive a full OEI payment. This will be achieved through four main channels:

      i. the relaunch of the Operations Manual in March, which aims to provide a comprehensive and easy-to-digest reference guide on how to run a branch;

      ii. the launch of a new online training module on back office processes, available by April;

      iii. the continuation of the Area Manager Operational Excellence visits to provide face-to-face guidance on these processes, building on the 7,343 branch visits completed to date; and

      iv. support through the Branch Support Centre (BSC) to deal with any queries that branches have on their payments. BSC staff will be given full training to manage these enquiries, alongside nominated contact points for subject

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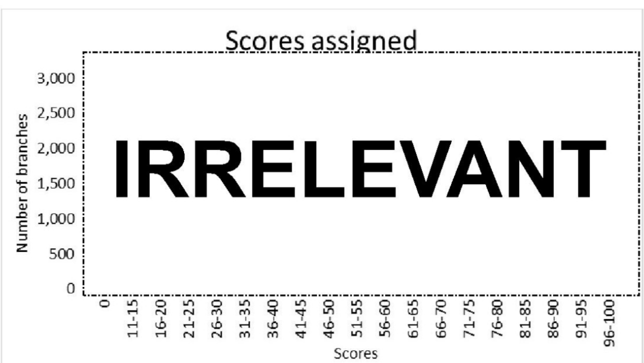
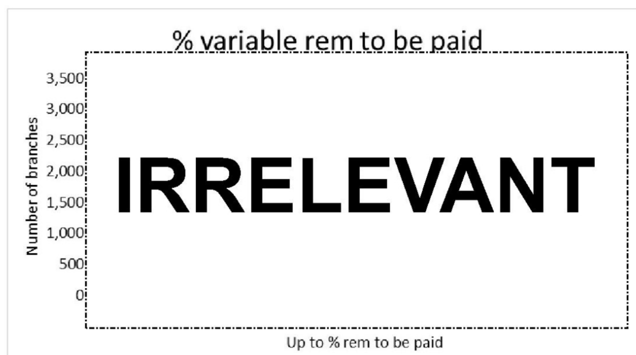
matter experts on any more complex questions. We will also publish a Frequently Asked Questions document on Branch Hub to seek to pre-empt the majority of simpler queries.

6. Alongside these two *hard* dependencies, the postmasters we have consulted have consistently raised the importance of note counters to enable them to accurately and efficiently process growing cash volumes. While in principle we could launch the OEI scheme without addressing this request, this will inevitably provoke criticism that we are not giving them the essential tools they need to do their job. Our recommendation therefore is that, subject to positive results from the 40 pilot branches, we commit to providing our c.3,500 largest banking branches with note counters alongside the launch of the OEI scheme. This would create a strong package of measures to both improve branch profitability and reduce discrepancies. An option for funding the costs of these note counters is set out below.

## What are the expected payments and financial implications?

7. Based on the scoring set out above, the charts below show the scores achieved across the network based on a recent month of data (November trading) and how this then translates to a variable remuneration increase. In summary, based on this snapshot of *current* performance, IRRELEVANT would receive a smaller uplift averaging IRRELEVANT




8. If this current performance were maintained for a full year, it would generate a total annual payment of c.£IRRELEVANT. If all branches achieved perfect scores every month, then the total annualised payment would be IRRELEVANT. Clearly we hope that this scheme, along with other proactive measures being taken, will improve performance. Our best estimate is a full-year figure of around IRRELEVANT which is consistent with the allocation for 2024/25 remuneration increases in the current Three Year Plan. The proposed September launch date set out below reduces the first year costs to IRRELEVANT

9. Improvements in these activities will help us to reduce our costs, in particular in the following areas (these are the total costs for each area rather than the estimated savings):

- IRRELEVANT for staff costs for dealing with transaction corrections, discrepancies and other related issues from postmasters;
- IRRELEVANT for branch discrepancies; and

1. The c.1,400 branches in the left-hand graph showing zero points are those that did not complete their trading period balance in the correct week. Around 1,200 of these did complete their balance within the month but in the wrong week.

- IRRELEVANT for interest costs from excess cash assuming current base rates of IRRELEVANT (these costs are currently running at IRRELEVANT pa based on the existing hedge at IRRELEVANT).

10. The scale of the cost reduction will depend on the behavioural response to the incentives alongside the impact of other measures, and will be tracked closely pre and post launch.

## When do we propose to announce and launch the new scheme?

11. We have committed to an annual cycle of remuneration announcements in March of each year detailing the rate increases for the new financial year. We therefore propose to announce details of the new OEIs scheme as the centrepiece of the forthcoming March 2024 announcements. However, rather than commencing the new payments from April, we would recommend delaying the actual launch of the scheme until September remuneration (August trading), for two reasons:
    a. to save IRRELEVANT budgeted remuneration increase, which we propose should be ringfenced to fund the deployment of note counters to IRRELEVANT, subject to evaluation of the results from the first 40 pilot branches. This will reduce opex and increase capex in next year's budget;
    b. to allow four months of 'dry running' with branches during which period we would share monthly data on their performance against the OEI metrics via Branch Hub, allowing ample time for them to understand how the scheme works and to thoroughly test and refine the support mechanisms detailed in paragraph 5.
12. In our March announcement we will indicate that the specific metrics and scoring mechanisms are subject to ongoing review, taking into account feedback from branches both during the 'dry run' period and through the subsequent months of live running.
13. Given the links to the wider budgeting process, we suggest seeking Board approval for this scheme (and any other remuneration changes for 2024/25 as outlined below) at the February Board meeting.

## What other 2024/25 remuneration changes do we expect to announce in March?

14. The other major remuneration changes we expect to include in the March announcements are as follows:
    - the standard CPI increase to Royal Mail and Parcelforce volume-based rates, expected to be worth IRRELEVANT based on current inflation rates of 3.9%;
    - the impact of the Royal Mail tariff changes expected to be confirmed within the next two months (the value of which are unknown at this stage);
    - the continuation of the Major Branch Support payment to IRRELEVANT for a further year, at a cost of IRRELEVANT (but accrued in the current financial year). This is designed to reduce churn in those critical town and city centre branches which are not yet benefiting from banking growth and mails automation; and
    - cost-based increases to fixed outreach payments IRRELEVANT
15. Further details of these increases and any other product remuneration proposals will be set out in February, in the context of the wider 2024/25 budget projections for remuneration and trading profit.