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Initial Complaint Review and Mediation Scheme

**Reply of Post Office Limited to Second Sight's Briefing Report - Part
Two**

[Date]

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through the Scheme**

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Final Draft

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Introduction

- 1.1 As part of the Initial Complaint Review and Mediation Scheme (**the Scheme**), Second Sight is engaged as a firm of forensic accountants to provide a logical and fully evidenced opinion on the merits of each Applicant's case.
- 1.2 On 21 August 2014, Second Sight's Briefing Report – Part Two (**the Report**) was ~~released sent~~ as a confidential document to a number of applicants and their advisors. The purpose of the Report was to describe and expand on common issues identified by Second Sight as being raised by multiple Applicants (**a thematic issue**). The aim being to provide general information that could then be applied in specific cases in the interests of efficiency.
- 1.3 Post Office has been unable to endorse the Report. It wrote to recipients of the Report immediately after its release setting out its reasons for this and committed to set out its detailed position on the issues raised in the Report. In the interests of transparency and with the overriding aim of assisting the resolution of complaints brought under the Scheme, Post Office has prepared this Reply in order to correct inaccuracies in the Report and to provide information that the Report omits.
- 1.4 The body of this Reply provides Post Office's detailed comments on each section of the Report. There are however a number of issues that reoccur throughout the Report which are summarised below.

Lack of thematic issues

- 1.5 A number of sections in the Report do not identify a thematic issue which could be of general Application to multiple applicants as opposed to matters that need to be addressed on a case by case basis. Where this arises, Post Office will address those issues in its case specific Investigation Reports.
- 1.6 Of the 19 sections in the Report, 9 sections do not identify a thematic issue namely sections 6, 7, 11, 12, 13, 14, 15, 19 and 20.

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Absence of conclusions

1.7 The majority of the cases in the Scheme turn on there having been a loss in a branch for which an Applicant was held liable. For a thematic issue to be of utility, it must help explain why a loss may have arisen or been attributed to an Applicant. The Report is largely silent on this critical issue. As it stands, there are a number of topics in the Report where "enquiries are on-going". A number of other sections set out the competing views of Applicants and Post Office but offer no view on whether either parties' position is to be preferred.

1.8 Of the 10 sections that identify a thematic issue, 5 do not reach a conclusion namely sections 8, 9, 16, 17 and 21. A firm conclusion would have assisted ~~Post Office and Applicants and~~
~~+Post Office.~~

Scope

1.9 The scope of the ~~Report and the~~ Scheme is to consider matters "concerning Horizon and any associated issues". Matters such as the Subpostmaster contract and other legal matters are not within the scope of the Scheme and are outside Second Sight's professional expertise.

1.10 The Report goes beyond the scope of the Scheme and Second Sight's expertise in sections 4, 18 and 22.

Missing evidence

1.11 The Report lacks in a number of places supporting evidence, source documents, examples or statistics to substantiate the conclusions it draws. It does not describe the overarching methodology used to examine the weight of evidence from different sources - this is most important where ~~a much of~~ the information provided by Applicants is anecdotal and ~~has yet to be investigated and tested. needs to be carefully assessed for credibility and accuracy.~~

1.12 At the time the Report was completed, Second Sight had investigated 21 cases submitted to the Scheme and completed

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~~rendered its~~ final Case Review Reports in 10 cases. Second Sight has received information from the approximately 150 Applicants to the Scheme, whereas in total there have been more than 450,000 users of Horizon since its inception in 2001. The Report is therefore based on the tested views of only 0.0003% of all Horizon users and cannot therefore be said to reflect general user experience.

1.13 The 2 sections of the Report that reach findings on thematic issues within the scope of Second Sight's expertise, (sections 5 and 10), are both unsupported by tested and credible evidence.

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This Reply

- 2.1 It is recommended that the reader familiarises themselves with Second Sight's Briefing Report - Part One (**the Part One Briefing**) which provides background information on Post Office's processes and procedures. This Reply builds on the information in the Part One Briefing.
- 2.2 Care should be taken when applying the Report and this Reply to individual cases. Not all of the information will be applicable in every case. Several of the topics are themselves multifaceted so even where an Applicant has raised a topic, not all aspects of that topic may exist in that case. Also, the specific circumstances of a case may show that a topic did not in fact have any effect on an Applicant.
- 2.3 In this Reply:
 - References to paragraphs and sections are to paragraphs and sections of the Report unless stated otherwise.
 - "Applicant" means an applicant to the Scheme whereas "Subpostmaster" means Subpostmasters in general, whether or not they have applied to the Scheme.
 - For ease of reference, where reference is made below to "Subpostmasters" or "Applicants" taking action in a branch, this action could, in most circumstances, also be taken by a Subpostmaster's assistant.
 - All other capitalised terms are defined in the Part One Briefing.

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Overview of Post Office's position

- 3.1 Nearly all Applications to the Scheme centre on there being a loss of cash from a branch that the Applicant does not consider that ~~he/she~~they caused or are liable for. The focus of the Report and this Reply is to help identify those issues that can cause such a loss and those that cannot.
- 3.2 In order to identify a loss of physical cash, an investigator needs two pieces of key information:
 - a. ~~They need to know~~How much cash should be in the branch as a result of the transactions processed in the branch. This information is provided by the branch accounts stored on Horizon.
 - b. ~~They need to know~~How much cash is actually in the branch. This is known by conducting a physical count of the cash on hand.
- 3.3 Any difference between the above two figures generates a "discrepancy" which may either be a shortage or a surplus.

Controlling the branch accounts

- 3.4 If cash is missing, the first stage of the investigation is to identify the day on which the cash went missing. The transactions for that day can then be reviewed for anomalies (see section 10 of the Part One Briefing) eg:
 - Transactions incorrectly recorded (such as withdrawals recorded as deposits);
 - Values incorrectly entered (entering £2000 instead of £200).
- 3.5 This is done to determine if the branch has made errors that would make the branch accounts inaccurate.-(item 1(a) above). This review must be done by the branch staff as only they will know the transactions done on that day and may recall the correct transaction details. Many branch errors (including the two examples above) are most easily identified in branch. They would

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not be evident to Post Office unless a complaint was made by a customer.

- 3.6 Post Office helps correct branch errors where possible by reconciling Horizon records against data collected on some transactions by third parties such as banks and government departments. Where Post Office detects an error through this reconciliation process, it issues a Transaction Correction to a branch notifying them of the error and correcting the branch accounts.
- 3.7 It has been alleged by some Applicants that they have been issued Transaction Corrections even when they were not at fault. Transaction Corrections are only issued where there is clear evidence of an error in branch. Where the cause of loss rests with Post Office or third party client Post Office absorbs that cost and it is not passed back to branch. This principle underlies the design of Horizon and all Post Office's back office and reconciliation processes.

Controlling cash movements

- 3.8 Save when it conducts an audit, Post Office does not have any direct knowledge of what physical cash is actually in a branch - only Subpostmasters have this information. For this reason, branches are required to:
 - Count the amount of cash in the branch daily and record this figure on Horizon as a cash declaration.
 - Count all cash and stock at the end of each trading period and record these figures on Horizon before making good any discrepancies¹.
- 3.9 If daily cash declarations are not made by a branch or declarations are made falsely (by declaring that there is more cash in the branch than there actually is) then it is impossible for Post Office, and will be very difficult if not impossible for a Subpostmaster, to:
 - Know if cash is missing;

¹ See paragraph 8.8 of the Part One Briefing regarding "making good" errors.

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- Identify the days on which cash has gone missing;
- Identify which member of staff may be the source of errors; or
- Locate the erroneous transactions that were the cause of a loss.

3.10 Daily accurate cash declarations are the most critical aspect of branch accounting, without which losses of cash, ~~being taxpayer money,~~ go unchecked.

3.11 For this reason, it is not acceptable to Post Office for Subpostmasters not to make accurate daily cash declarations. Subpostmasters habitually failing to make cash declarations may find their contracts terminated. Post Office also prosecutes those Subpostmasters who dishonestly make false cash declarations. It is not an excuse to say that a Subpostmaster was poorly trained or received inadequate support in this regard. The need for daily cash declarations is known by all Subpostmasters and is easily done – there is no specialist training or support required (albeit that both do exist). Post Office does not accept that there is any excuse that could justify committing the criminal offence of rendering a false account.

3.12 In the context of the Scheme, there are a number of cases where accurate cash declarations have not been made. Many of these Applicants have challenged Post Office to identify the cause of losses in their branches which they ~~had hidden by falsely accounting then subsequently hid through FA~~. As explained above, identifying the specific source of the losses is not possible where an Applicant has failed to follow the simple but critical task of making accurate daily cash declarations. They are, in this situation the architect of their own problem.

3.13 Subpostmasters are contractually liable for any losses hidden or caused by their inaccurate record keeping whether due to error, dishonesty or otherwise. It is also a well-established common law principle that an agent (~~like e.g.~~ a Subpostmaster) is

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liable to pay to his principal (e.g. being Post Office) any sum declared in his accounts.

Responsibility for losses

3.14 A number of Applicants have accused Horizon of inaccurately recording the transactions processed at their branch (item 1(a) above) which they say shows that they were not liable for the losses in their branches. To date, Post Office has been provided with no evidence by either an Applicant or in the Report of that presents any doubt that Horizon's has failureed to record transactions accurately.

3.15 The Report looks to identify thematic points where Second Sight considers that Horizon may be flawed. As explained in this ReplyHowever, these points are either ill-explained, un-evidenced or are proven not to be the cause of losses in branches.

3.16 Absent any doubt over the integrity of the branch accounts produced by Horizon, Post Office considers it a-fair starting position to assume that if a loss has occurred then it has been caused in the branch and is something for which, in most circumstances, a Subpostmaster is liable to make good. This reflects the core tenet of the Subpostmaster Contract that Subpostmasters are liable for any loss caused by their carelessness, negligence, dishonest conduct or error.²

3.17 Post Office remains committed to fully and open-mindedly investigating every allegation levied made about Horizon through the Scheme. It is in its our interest as well as the interest of the 6,000 serving Subpostmasters who have not applied to the Scheme to identify an issue if one exists. However, Post Office is confident that there are no systemic problems with branch accounting on Horizon and all existing evidence overwhelmingly supports this position.

² Clause 12, Section 12

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Post Office's response to section 4 – The Contract between Post Office and Subpostmasters

- 4.1 Section 4 of the Report concerns the contract between Post Office and Subpostmasters dated September 1994 (as revised over the years) (**Contract**). It considers (1) the potential impact of some of the terms and conditions and (2) issues relating to notification of the Contract terms to Subpostmasters.
- 4.2 An assessment of the Contract is outside the scope of the Scheme which was to consider "*Horizon and associated issues*". Second Sight has no mandate to consider the Contract and the Report contains a number of statements that are incorrect. These errors arise from the fact that Second Sight are not lawyers, but forensic accountants, and any assessment of the Contract can only be undertaken against legal principles. For this reason, no weight should be placed on this section of the Report as it reflects only Second Sight's lay opinion on matters where they have no expertise or experience.
- 4.3 To help avoid potential confusion ~~alleviate the confusion created by the Report~~, Post Office sets out the correct position in respect of the Contract below.

Impact of selected terms and conditions

- 4.4 At paragraph 4.5 the Report sets out selected sections of the Contract. Whilst these provisions do reflect the terms and conditions as stated within the Contract these are selective and not reflective of the Contract as a whole. In addition, the ~~Part Two~~ Report does not appear to take account of~~have considered the~~ other documentation that is incorporated into the Contract such as manuals, booklets and operational instructions issued by Post Office from time to time.

Fairness of the Contract

- 4.5 Paragraphs 4.4 and 4.6 both make the same conclusion that "*from a business perspective*" the contractual provisions referred to

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above (in particular Section 12 requiring the Subpostmaster to make good losses) operate to the detriment of a Subpostmaster.

- 4.6 The Report comments that under the Contract (presumably again in reference to clause 12, section 12 though this is not clear in the Report) there is a transfer of "risk" to the Subpostmasters. The suggestion being that this is somehow unfair on Subpostmasters.
- 4.7 First, the Contract is a business to business arrangement. Save in a few very narrowly defined areas (which are not applicable here), there is no general principle at law of whether the Contract is "fair" or not. The Contract terms apply as they are written and Post Office consider them to be balanced and fair. The analysis in the Report ~~has failed to~~ does not appreciate this point.
- 4.8 Second, Subpostmasters are agents and Post Office is their principal. At law, agents owe duties to their principals including the duty to act in good faith, to render accurate accounts and to make good any losses they cause. Section 12 of the Contract simply reflects these legal principles - it does not transfer any additional risk to Subpostmasters.
- 4.9 Third, when considering this issue no reference is made in the Report to any other similar agency agreement or benchmarks that may provide a view on what is common practice. In Post Office's experience, the terms of the Contract are broadly similar to those used in franchising arrangements across the UK.
- 4.10 Fourth, the Report does not appear to consider the role of NFSP. Any variations to the Contract are discussed with NFSP prior to being implemented. This is in clear contrast to the position set out in the Report that Post Office arbitrarily imposes its terms and conditions on Subpostmasters.
- 4.11 Whilst the Contract does place responsibilities on Subpostmasters (as well as Post Office), these are not commercially or legally unfair. In any event, the Contract reflects the basis on which Post Office and thousands of Subpostmasters have successfully conducted business for decades.

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It is not now open to seek to retrospectively change that foundation. At a number of points the Report has alluded to "duties" on Post Office that do not exist in the Contract. Post Office acts in accordance with the Contract and expects Subpostmasters to do the same.

Subpostmaster's understanding of the Contract

- 4.12 The Report suggests that Subpostmasters may not have reviewed or fully understood the terms before entering the Contract. As a result, the Report states, at paragraph 4.7, that Subpostmasters are unable to mitigate "risks" that they may face.
- 4.13 Post Office disagrees with the conclusion reached in the Report. In addition, this conclusion is not supported by any evidence.
- 4.14 The Contract that is entered into between Post Office and Subpostmasters is done so freely and at arm's length. Ultimately, it is for the Subpostmasters to choose whether they enter into the Contract or not. The Report does not provide any examples where Post Office is accused of using undue influence or other unfair behaviour to acquire the agreement of individual Subpostmasters to the Contract - and it is strongly denied that any such improper conduct has occurred.
- 4.15 The Report provides no evidence that Subpostmasters do not understand the Contract. If the view being taken in the Report is from a business perspective (whether Post Office or a Subpostmaster) the provisions are very clear and written in plain English.
- 4.16 In any event, it is a well-established legal principle that a person who agrees to a contract is bound by its terms even if he does not have a copy of those terms, has not read them or does not understand them. Post Office cannot be responsible for an Applicant Subpostmaster who may not have taken the time to read the Contract.
- 4.17 The Report also notes that Post Office does not recommend that Subpostmasters take legal advice. There is no obligation on Post Office to make this recommendation. It is however open to

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any Subpostmaster to take legal advice on the Contract at any time.

4.18 The report also appears to discount that the Applicants are business people and from a business perspective, they would be used to agreeing contracts and should be aware of the risks of agreeing to a contract without legal advice.

Notification to Subpostmasters of the Contract terms

4.19 Paragraphs 4.8 to 4.11 state that Post Office does not provide a copy of the Contract to Subpostmasters. Post Office does not see what evidence this conclusion is based upon. It appears to be based on the fact that a Subpostmaster does not recall receiving the Contract or cannot produce a copy now. This does not mean that the Contract was not provided. Given the age of some of the cases in the Scheme, it is not surprising that recollections are hazy and that some records are now not available.

4.20 It is open to Subpostmasters to request a copy of the Contract throughout negotiations when seeking appointment and from Post Office's Human Resource Service Centre if they have misplaced or lost a copy.

4.21 It is also Post Office's standard operating procedure to ensure that the Subpostmasters have a copy of the Contract no later than the day that they commence their position.

4.22 Paragraph 4.10 highlights that it is common practice for new Subpostmasters to sign an "Acknowledgement of Appointment" without a copy of the Contract. It is common practice that a separate document will be signed rather than the full Contract. As a point of law, terms and conditions can be incorporated into a contract by reference to another document that is not signed. Also, as noted above, Subpostmasters are business people and will have had opportunity to request and review the Contract prior to signing. Also they would have had opportunity to take legal advice on the Contract prior to entering into it. Subpostmasters would therefore have had a number of opportunities to be aware of the specific contractual provisions they were agreeing to.

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Conclusion

4.23 The Report states that the Contract was considered "*from a business perspective*". It is not clear what this means in light of the criticism in the Report. Post Office would suggest that this should mean that Subpostmasters, as business people, enter into the Contract of their own choice having had opportunity to seek legal advice should they wish to do so.

4.24 Post Office does not see how this section provides greater clarity on the issues in dispute between Applicants and Post Office.

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Post Office's response to section 5 – Automated Teller Machines (ATMs)

- 5.1 Section 5 of the Report raises various issues concerning the accounting in branch for ATM transactions.
- 5.2 The Report does not clarify which precise part of the ATM accounting process is under consideration by Second Sight. In broad terms, the accounting process breaks down into three elements:
 - a. Loading – Cash for the ATM is sent to the branch by Post Office and is loaded by the Subpostmaster into the ATM. This requires the recording of the ATM Cash as part of the branch's stock.
 - b. Cash dispensed – the amount of cash dispensed by an ATM is recorded daily on Horizon – see further below.
 - c. Exceptions – rejected cash and retracted cash – see further below.
- 5.3 From the content of the Report, Post Office believes that Second Sight has focused primarily on the processes for the recording of cash dispensed from the ATM however other issues are touched on also.
- 5.4 In short, nothing in this section of the Report gives rise to any issue that could cause a loss of cash in a branch. The Report does highlight a few areas where Applicants have claimed to struggle with accounting for ATM transactions but the design of the accounting process and the safeguards put in place by Post Office mean that even a failure to account for ATM transactions will, save in a few minor areas (highlighted below), not cause a loss to a branch.

Out of sync / air gap

- 5.5 The Report focuses on the situation where cash is dispensed from an ATM. The process for accounting for dispensed cash is set

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out at paragraph 5.27 of the Part One Briefing. In short, on a daily basis (or on a Monday following a weekend) the Subpostmaster prints a receipt from the ATM showing the amount of cash dispensed. This cash dispensed figure is then entered into Horizon by the Subpostmaster.

- 5.6 Simultaneously, the amount of cash dispensed is also automatically transmitted to BOI by the ATM. This means that there are two parallel records kept of the cash being dispensed by the ATM: one by the Subpostmaster on Horizon and one by BOI.
- 5.7 The Report notes that there are situations when these two systems can become out of sync with one another, with one record showing more or less dispensed cash than the other record. This could be caused by the Subpostmaster entering the wrong figure on Horizon.
- 5.8 What is not highlighted by the Report is that even if the amount of money dispensed by an ATM as recorded on Horizon by the Subpostmaster is different from the amount actually dispensed as recorded by BOI, therefore resulting in the records being "out of sync", this would not result in there being a loss to the branch. This is a pure accounting error by the branch.
- 5.9 There is a subsequent reconciliation of the Horizon figure against the BOI accounts. This means that any error on the Horizon account as to the amount of cash dispensed by the ATM would be picked up within a matter of days and corrected by way of a Transaction Correction to the branch.
- 5.10 As a result of this process, there is no difference in the amount of cash held on site. Indeed, the above accounting processes do not require anything to be done with the physical cash at all.
- 5.11 Simply because the accounts may be "out of sync" does not mean that there is a loss suffered by the branch. In summary, the air gap / out of sync issue cannot be a cause of loss in branch.

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Complexity of accounting for dispensed cash

5.12 At paragraph 5.4 the Report states that the Post Office system for operating ATMs is "*a complex arrangement, requiring greater human intervention... than that typically needed in most high street banks*". The Report does not specify which part of the branch accounting process is considered more complex, however given the focus on the "out of sync" issues it seems that the Report is levying this allegation at the accounting process for dispensed cash (see above).

5.13 The Report's conclusion is not supported by any evidence and does not outline the differences between Post Office's and a bank's processes save to say that banks' ATMs are fully computerised.

5.14 At various points, and particularly paragraph 5.18, the Report suggests that Applicants also found it difficult to account for cash being dispensed from ATMs. Little evidence is presented to support this view.

5.15 As described above, the ATM automatically records the amount of cash dispensed. The only part of the process that is manual is the need for the Subpostmaster to take the cash dispensed figure from the ATM and enter into onto Horizon. Second Sight has adopted the phrase "Air Gap" for this manual interaction. As far as Post Office is aware, it is not a phrase used by any Applicant.

5.16 Within this accounting process, no calculation or counting is required – it is literally typing a single figure into Horizon on a daily basis. Given the absence in the Report of any explanation or justification for the view that this is "*complex*", Post Office ~~does not accept cannot understand how that this process can be called is "complex". or how this cannot be understood by Applicants.~~

5.17 The Report appears to rely on a number of extracts from Post Office's Operations Manual to show that the above accounting method was too confusing for some Applicants. Paragraph 5.13

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states that the out of sync problem described above, was common place prior to February 2008. However, the Report sets out the opinion, at Paragraph 5.15, that the instructions from the Operations Manual represents an example of the complex instructions and a cause of confusion. Paragraphs 5.13 and 5.15 are therefore a contradiction of one another – the first saying the problem pre-dated 2008, the other saying the problem resulted from the 2008 update.

5.18 The Report does not describe any instructions provided prior to the February 2008 Operations Manual or any subsequent updates. No assessment is made as to any change in the reporting of problems in relation to ATMs (and specifically not understanding the instructions) before or after the February 2008 Manual update and in particular whether or not there was an increase or reduction of the potential for errors. This ~~would appear to be a~~ fundamental assessment and consideration ~~that~~ has not been made in the Report. Together with the fact that no evidence is provided to confirm how many Applicants did attribute errors to these (or any other) instructions, whether before or after February 2008, means there is no evidence to support the Report's view that the ATM accounting procedure was too complex.

ATM Support

5.19 The Report notes that Applicants have alleged that the Helpline repeatedly told them that in respect of the "out of sync" error the "problem would sort itself out". It also states at paragraph 5.19 that the advice from the Helpline was inadequate and misleading. There is no evidence provided to support either allegation. The advice provided needs to be assessed on a case by case basis as there is no evidence that there is a wider issue with the advice provided; it has not been shown to be a thematic issue.

5.20 Even if the advice provided was that an error would "sort itself out", in light of the reconciliation between Horizon and BOI (as described above) if there was an "out of sync" problem it would be corrected by a Transaction Correction. This would prevent the

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build-up of any accounting shortfalls. As explained above, there is no loss caused to a branch by an "out of sync" issue as the overall cash in branch relating to the ATM remains the same.

5.21 Overall, the assertion that the support provided was inadequate has not been supported by any evidence or logical reasoning.

Weekend trading

5.22 Paragraph 5.18, which considers trading over weekends, appears to have no relevance to the cause of losses on the ATM. Post Office is not aware of any specific issue with operating an ATM ~~off-at~~ at weekends.

Power and telecommunication issues

5.23 Paragraph 5.20 of the Report states that many Applicants have commented on the impact of power and telecommunications failures on the ATM. The Report acknowledges that, even when they have dates of power or telecommunications failures, Applicants cannot clearly link them to specific deficiencies in their branches.

5.24 There are standard recovery processes in place to ensure that no data is lost or corrupted. This recovery process was reviewed in detail by Second Sight in their Interim Report and found to work. Post Office remains confident that branch accounts will not be corrupted due to a power or telecommunications failures.

5.25 Despite this, the Report speculates that the need to re-boot the ATM by either the Subpostmaster or BOI could "introduce a possible risk of data loss or corruption". This comment is not supported by any evidence either from a specific Applicant's case or general evidence that such a problem may exist.

5.26 Post Office has not been provided with evidence that contradicts the assurances provided by Post Office that data cannot be corrupted. Post Office is not aware of this "evidence" ~~and it is not~~ If it was credible, one would expect that evidence to be set out in the Report.

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Retracts

5.27 Paragraphs 5.21 to 5.25 discuss failed cash withdrawals. As paragraph 5.22 and 5.23 state, if cash dispensed is not physically removed then after a period of time the cash will be retained by the ATM. This is known as a retract. It can occur for a number of reasons but often because the customer gets distracted. It is also possible that retracts can be subject to fraud by customers. The Report indicates that Subpostmasters might be liable for losses caused by this fraud. This is correct where Subpostmasters have failed to account for retracts correctly. Provided the accounting is done correctly, a Subpostmaster will not be liable for any loss caused by retract fraud.

5.28 The accounting process for retracts is as follows:

- a. Each working day, a Subpostmaster must check the ATM Bank Totals receipt (which is generated by the ATM) to see if any retracted transactions have taken place. The receipt will show the number of retracts.
- b. If any retracts have taken place, the Subpostmaster must physically remove the retracted notes from the ATM (which are stored in a separate part of the ATM from other cash).
- c. For all retracted cash removed from an ATM, the Subpostmaster must count and report on Horizon the total value of retracted cash on the same day (using the ATM Surplus Cash button on Horizon). If a retract occurs when the Post Office branch is closed it should be removed and reported on the next working day.
- d. Once reported on Horizon, the retracted cash should be placed in the branch safe and forms part of the cash holdings of the branch.

5.29 Customers' accounts will be debited even though they did not remove their cash. This is often re-credited but it is an issue for the customer and their bank, although Post Office will do what it can to assist both to resolve this issue. At this

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point, the branch accounts will balance as the amount of cash physically dispensed (including any cash subsequently retracted) will match the cash dispensed figure on Horizon and the amount of cash in the retract cassette will have been counted and added to the branch accounts.

- 5.30 Retract fraud occurs where a customer conducts a withdrawal transaction from their own bank account using an ATM. When the cash is vended, the customer looks to remove the middle notes, leaving the top and bottom notes behind, thereby hoping to trick the ATM into believing that the cash has not been taken. The ATM then retracts the remaining cash back into the machine, believing that it has retracted the entire sum withdrawn. The fraudulent customer's intention is that when the bank checks the retract records for the ATM in question, it sees that there was a retract recorded against the customer's withdrawal transaction and would then fully re-credit the customer's account.
- 5.31 Provided the Subpostmaster follows the above procedure in relation to retracts, he will not be liable for any ATM cash loss caused by retract fraud.
- 5.32 Post Office provides to BOI details of the amount of each retracted cash transaction as part of its weekly ATM balances recorded on Horizon. BOI uses that information to look for a match between the actual amount of retracted cash removed from the ATM and the amount of the original cash withdrawal transaction. If there is a match, then this will indicate that there has been no retract fraud and the full amount will typically be re-credited to the customer. If there is a discrepancy, then BOI may undertake further investigations into the customer's activity.
- 5.33 As long as Post Office can provide the daily retract declarations from Horizon then any loss caused by any retract fraud does not fall on the Subpostmaster.
- 5.34 If a Subpostmaster does not declare a weekly ATM balance through Horizon, which includes the amount of any retracted cash, then Post Office cannot provide that information to BOI. As BOI has

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not been provided with balancing information it is unable to determine whether a retract was fraudulent. The full amount of the cash withdrawal re-credited to the customer is therefore charged on by BOI to Post Office.

5.35 Where Post Office is charged by BOI, it passes on this charge to the Subpostmaster by way of a Transaction Correction where the weekly ATM balance, including any retracted cash records, are not available because of the Subpostmaster's failure to follow proper accounting processes.

5.36 It should be noted that where the retract was not fraudulent, the correct amount of cash will have been retracted into the ATM. Even if the Subpostmaster has not properly accounted for this cash on Horizon, the retracted cash will still be in the branch (either in the branch's cash holdings or still in the ATM) as surplus cash. This surplus cash will offset any Transaction Correction for failing to follow proper accounting procedures.

5.37 Where retract fraud has occurred, then the amount of surplus cash recovered from the ATM will be less than the amount of the original cash withdrawal transaction. This discrepancy will fall on the Subpostmaster if they have not followed the proper accounting procedures.

5.38 The Report does not suggest there is any failure in the above procedure that may cause an unwarranted loss to a Subpostmaster. Post Office therefore remains confident that provided the above process is followed by a branch, a Subpostmaster will not be liable for loss caused by retract fraud. However, should they not follow the above process, then they may be liable for some or all of the cash lost to the fraud. Post Office considers that this allocation of responsibility for preventing retract fraud is fair and Subpostmasters can avoid all risk altogether by following the above simple accounting process.

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Other frauds

5.39 Post Office accepts that there are other forms of fraud that may be occurring. However, it we are is not aware of any form of fraud (including retract fraud) that creates a loss to Subpostmasters, provided they follow the correct accounting procedures.

Conclusion

5.40 Overall, provided a Subpostmaster follows the appropriate procedures they will not be liable for any ATM loss due to an "out of sync" problem or retract fraud. Post Office does not agree that the instructions and support in relation to ATMs is inadequate. No evidence is provided to support this position nor have the large number of ATMs across the Post Office network that are operated without concern appear to have been considered. This would support the position that the operating practices for ATMs are clear, understood and work in practice.

Post Office's response to section 6 – Motor Vehicle Licences

- 6.1 Section 6 of the Report considers the issuing of Motor Vehicle Licences (**MVL**). The Report itself notes that only a small number of Applicants reported problems concerning processing MVL. It is not therefore clear that this can ~~properly therefore~~ be considered a system wide issue of general application.
- 6.2 Paragraph 6.1 describes a problem encountered (by what Post Office believes to be a single Applicant) when form V11C (the form used by customers to renew their MVL tax discs) was misprinted with the incorrect barcode. Form V11 is not produced by Post Office but by the DVLA and therefore this was an external error. The Report states that the effect was that a sale was recorded as a 12 month tax renewal rather than the 6 month tax disc as was sold. The Report states that whilst the customer would have paid for and received a 6 month tax disc, the accounts would have recorded a sale of a twelve month disc

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and, as a result, there was a potential liability to the Subpostmaster for the additional 6 months.

6.3 This is incorrect. The barcode on the V11C form does not define the duration of the tax disc but the overall cost whether taxing a vehicle for 6 or 12 months. A V11C is printed with tick boxes for the customer to confirm whether they would like to tax a vehicle for 6 or 12 months. Upon scanning the V11C, which identifies the registered vehicle, Horizon will prompt the user to enter whether the customer wants a 6 or 12 month tax disc. If the barcode printed was incorrect this could lead to a charge based on a different vehicle, which could be potentially more or less than the appropriate charge if the vehicle identified by the barcode is in a different tax band to the customer's actual vehicle.

6.4 If there is an error with a barcode, it would be an issue with the tax banding not whether a vehicle is taxed for 6 or 12 months. This issue could benefit or disadvantage the customer. However, Horizon would invite payment at the level requested by the barcode. Provided that payment was taken for the amount requested by Horizon the branch would not suffer a loss as there is no loss or gain from the transaction from the branch's and Post Office's perspective. Whilst this issue is clearly not desirable (and Post Office would offer all possible assistance to the customer to correct any error on the DVLA issued V11C form), this issue does not impact on branch accounting.

6.5 Paragraph 6.2 speculates that if this type of discrepancy occurred, resulting in a loss for the branch which the Subpostmaster would be liable for, the amounts could be significant. There appears to be no evidence to support this assertion. This appears to be a one off incident, created by a barcode that was created by a third party, the DVLA. As this issue is so specific to a particular customer's Applicant's circumstances, Post Office cannot see how this can be classed as a thematic issue affecting Applicants generally.

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Post Office's response to section 7 - National Lottery

7.1 Section 7 concerns National Lottery transactions which are described in more detail at paragraph 5.35 of the Part One Briefing. In particular the Report highlights alleged problems that Subpostmasters may have in relation to (1) scratchcards and the activation of them and (2) sales continuing outside of Post Office hours of Lottery products in a connected retail shop resulting on the Horizon and Camelot terminals being "out of sync".

Activation of Scratchcards

7.2 Paragraph 7.2 states, correctly, that before February 2012 any Lottery scratchcards received by a branch had to be manually "activated" on Camelot terminal and then remmed in to Horizon. This process is described in more detail at paragraph 5.42 of the Part One Briefing.

7.3 Paragraph 7.3 of the Report describes how a branch could become "out of sync". This means that the activation of scratchcards on the Camelot terminal did not reflect those remmed in on Horizon. This would result in either a surplus or a deficiency of scratchcard stock in the branch accounts. To remedy this error, Post Office and Camelot conducted daily reconciliations of the data on the Camelot terminal and on Horizon. Where there was a discrepancy, a Transaction Correction would be issued to the branch.

7.4 Any errors that occurred through the failure to activate or rem in scratchcards were errors that occurred in branch due to a failure to follow the correct procedure and therefore were a Subpostmaster's responsibility.

7.5 However, the effect of not remitting in scratchcards into Horizon will not in itself create a loss. The physical scratchcard stock will still be in the branch as it must have been delivered to the branch for it to be activated on the Lottery terminal. The Transaction Correction only increases the

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amount of scratchcards shown in the branch accounts to reflect the amount actually on hand.

- 7.6 If the scratchcards have been sold but not remmed into Horizon, the branch would show a negative stock value for scratchcards (as each sale reduces the stock line in the accounts even if this goes below zero). The subsequent Transaction Correction will therefore increase the scratchcard holdings, cancelling out the negative figure and bringing the accounts back into balance.
- 7.7 The opposite effect will happen if scratchcards have not been activated on the Lottery terminal but remmed into Horizon.
- 7.8 In summary, it is clear that ~~(1)~~ this issue is caused by errors in branch for which Subpostmasters are responsible but that in any event ~~(2)~~ this issue cannot be a source of actual losses.

Support

- 7.9 At paragraph 7.6 the Report states that the problems encountered by the Applicants (prior to procedural improvements described at paragraph 5.43 of the Part One Briefing) were exacerbated by the Helpline which ~~was~~ ~~were~~ not able to offer assistance. Post Office is not aware of the specific calls or incidents that the Report is referring to which are alleged to demonstrate a thematic failure to provide adequate advice.
- 7.10 This is ~~very much~~ an issue that will need to be considered on case by case basis depending on the advice provided to an individual Applicant. However, as noted above, the reconciliation process conducted by Post Office means that regardless of advice given by the Helpline, any error would be corrected in due course.

Out of hours sales

- 7.11 Paragraph 7.2 of the Report describes an alleged problem relating to the syncing of sales that take place "Out of Hours". Sales of Lottery products (as described at paragraph 5.39 of the Part One Briefing) may continue while a connected retail shop is open but the Post Office counter is closed however the branch

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needs to ensure that any cash taken for any "out of hours" sales is transferred from the retail shop to the branch cash holdings the following day.

7.12 The value of the "out of hours" sales (and any other sales) will be automatically sent to Horizon each day by way of a Transaction Acknowledgement which will increase the cash position in the branch's accounts. The amount of cash to be transferred from the retail side to the Post Office side is easily identified as the figure is displayed on the Transaction Acknowledgement. If a Subpostmaster does not transfer the physical cash from the retail side into the branch for these sales, this will produce a cash shortage. The Subpostmaster will be liable for this cash shortage at the end of the trading period.

7.13 Paragraph 7.7 of the Report highlights an alleged "complication" occurring on the final Wednesday evening of the monthly trading period for those branches operating Lottery terminals. This is reference to the trading period reconciliation completed on a monthly basis. Rather than process the reconciliation on a Wednesday evening as they would normally do, Subpostmasters with Lottery terminals have to first accept the Transaction Acknowledgement sent over night and complete the reconciliation as a matter of priority the following morning. The Report states that this process was not always provided by the Helpline.

7.14 Post Office has not seen any evidence to support this assertion and ~~would highlight that Second Sight~~ has been provided ~~with~~ call logs relating to individual ~~the~~ Applicants' cases. However, no specific calls are referenced ~~to~~ in support ~~of~~ this statement.

7.15 In fact, branches operating a Lottery Terminal needed to make daily cash declarations (see paragraph 8.2 of the Part One Briefing) like all other branches. As Lottery sales data is sent overnight, Lottery branches are instructed to conduct their cash declarations and end of trading period balances (see paragraph 7.45 of the Part One Briefing) first thing in the morning after the Lottery data was received. This was not therefore a

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complication but an adjusted daily process for branches with Lottery terminals.

7.16 In practice, some branches chose not to follow "next day" guidance and may have conducted balances several days later. Post Office operational instructions have however always provided for next day accounting.

7.17 In summary, any loss arising from "out of hours" issues highlighted in the Report will arise as a result of an error in the branch for which a Subpostmaster is liable.

Conclusion

7.18 Procedures have evolved to assist Subpostmasters and reduce the number of Transaction Corrections that are necessary in relation to scratchcards, especially in relation to the activation of them. However, the "out of sync" affect created by either incorrect activation or non-activation of scratchcards or not correctly recording the out of hours' sales are errors that arise within branch. The errors were not due to either Post Office or Horizon and therefore any liability appropriately remains with the Subpostmaster if it arises.

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Post Office's response to section 8 – Training, Support and Supervision

- 8.1 Section 8 principally considers the training on Horizon and branch accounting provided to Subpostmasters by Post Office. Currently, training for Subpostmasters consists of a mixture of classroom training and in-branch training. Further training is available upon request and there is a well-developed support network including the NBSC, managerial support and Field Support Advisors. This training and support is described in more detail at section 4 of the Part One Briefing.
- 8.2 The Report comments that the training was adequate in relation to "Business as usual" transaction processing but was weak in relation to the end of day, end of week and end of trading period balancing. In addition, the Report states that there was no consideration given to dealing with discrepancies, how to identify the root causes of problems and how to deal with Transaction Corrections.
- 8.3 These views appear to be based entirely on the anecdotal information provided by Applicants in their CQRs. As noted in the introduction to this Reply, ~~the credibility of~~ that information remains largely untested. Post Office has not been asked to provide any training materials for review nor has the Report established any industry standard or contractual benchmark against which to judge Post Office's performance. The limited analysis used to support the Report's conclusion is considered below and shown to be incorrect.
- 8.4 Given that the Report has presented no evidence or analysis that shows that Post Office's standard training is defective, Post Office stands by its training practices as being effective. Post Office considers that the training and support that is provided is fit for purpose and adequate to meet the needs of the large majority of Subpostmasters. This is proven by the thousands of Subpostmasters who are successfully operating Horizon having received the training from Post Office.

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8.5 There may of course be specific cases where training and support has not been provided to Post Office's usual standards (which is not impossible given the thousands of Subpostmasters trained and supported by Post Office over the years) but these situations will be considered on a case by case basis and are not reflective of any general thematic issue.

Move to Horizon

8.6 At paragraphs 8.3 and 8.4, the Report finds that many Applicants found that discrepancies began to occur when they moved to Horizon. The conclusion reached in the Report is that this was due to a lack of understanding of how the system was due to operate and be used, meaning they were insufficiently trained, had not been able to train their staff properly or there were issues with the new screen-based processes.

8.7 Post Office does not agree with this conclusion and it appears to be unsupported by any evidence that fewer mistakes were made prior to the introduction of Horizon. Transaction records are not available for the pre-Horizon period and it is not possible to test the conclusion which is put forward. It therefore appears that the Report has accepted Applicant's anecdotal recollection of events without any corroborating evidence. Paragraphs 1.11 - 1.13 in the introduction to this Reply highlights the deficiencies in this approach.

ATMs, Lottery transactions, MVL foreign currency or other specialist products

8.8 At paragraph 8.6 the Report highlights that Applicants considered that the Post Office trainers and Line Managers were weak in relation to dealing with ATMs; Lottery transactions; Motor Vehicle Licences; Foreign Currency and other products.

8.9 There is a lack of evidence to support these alleged comments from Applicants. Due to document retention policies training records for a number of Applicants are no longer available. There also appears to be no contemporaneous evidence that Applicants were not provided with adequate support by trainers

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or line managers whether in relation to ATMs, Lottery transactions, MVL foreign currency or other specialist products. If there was a lack of understanding in relation to these aspects Post Office would expect the Subpostmasters to request further training or otherwise seek assistance through NBSC.

Training Needs Analysis

8.10 Training support is provided through various means including the NBSC and managerial support. In addition, training materials are provided on a regular basis and further training can be requested by Subpostmasters.

8.11 The Report notes at paragraph 8.7 that further training was delivered in accordance with user demand rather than being determined by a Training Needs Analysis. This is not correct. When Subpostmasters complete their training there are follow up reviews at one, three and six monthly intervals. In addition to confirming that the business is operating as it should be there is an analysis on the Subpostmasters' understanding. If there are any gaps, these are highlighted and further training can be provided. After this stage there is a reasonable assumption that the Subpostmaster will be reasonably competent, with the support network highlighted above, to operate Horizon. ~~There should not be the need to periodically check the knowledge of Subpostmasters.~~ Subpostmasters are operating a commercial business and can request additional assistance and training when required.

Training assistants

8.12 As is made clear within the Contract (at section 15, paragraph 7) it is a Subpostmaster's responsibility to train his/her staff. Nevertheless, the Report criticises Post Office at paragraph 8.7 for not operating a "quality control function" to ensure that branch staff are properly trained by Subpostmasters.

8.13 The Report seeks to impose on Post Office a responsibility which is not stated in the Contract (see paragraph 4.11 of this Reply).

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8.14 ~~In fact, A-~~any failure by a Subpostmaster to train their staff adequately could be the reason for the losses or increase in discrepancies however any resulting losses would be due to the Subpostmaster's error and he would be liable for them (under section 12, clause 12 of the Contract).

8.15 In any event, Post Office could not operate the quality control function proposed by the Report. Each Subpostmaster, ~~as an independent business person~~, is free to employ whoever they wish (subject to registering them with Post Office) as Assistants and to give their employees whatever tasks they wish. ~~It may be that some employees are tasked to manage all aspects of branch accounting, whereas others may only have much more limited roles. There is therefore no universal training regime that could be applied to assistants and which could be centrally monitored by Post Office given the range of roles assistants fill.~~

8.16 Furthermore, Post Office cannot monitor the performance of individual assistants ~~it does not engage or employ (as Post Office employees are not located in agency branches)~~, only Subpostmasters can do this., ~~and so there is no way for Post Office to respond to the training needs of assistants as it does not know what they are.~~

8.17 Post Office agrees that a "quality control function" should be applied to assistants however this should be ~~undertaken operated~~ by Subpostmasters and not Post Office. Indeed, in a number of cases, losses appear to have stemmed from Applicants' failure to exercise any "quality controls" over the actions of their staff.

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Post Office's response to section 9 – The Helpline

9.1 Section 9 concerns the assistance provided by the Helpline to the Applicants. Post Office operates a number of helplines including the Horizon Help Desk and Finance Services Centre. It is presumed that the Report is referring to the NBSC. More detail on the Helpline can be found at paragraph 4.2 of the Part One Briefing.

9.2 The following criticisms of the Helpline are listed in the Report:

- a. Difficulty contacting the Helpline due to limited availability;
- b. Unhelpful, script based responses;
- c. Many calls were afforded "Low Priority", including those relating to balancing problems and discrepancies;
- d. Contradictory advice that revokes previous advice.

9.3 This section of the Report repeats allegations of Applicants. Those allegations appear untested (see paragraph 1.7 of the introduction to this Reply) and the Report reaches no conclusion at all. On this basis, Post Office cannot understand how this topic is considered a thematic issue. Nevertheless, the allegations presented in the Report are addressed below.

Difficulty contacting the Helpline due to limited availability

9.4 Post Office has previously acknowledged that as changes were made to standard operating practices over the years there have been periods where the Helpline could be difficult to contact. Changes were made, especially at the end of trading periods, and the hours that the Helpline was available for was extended.

9.5 Currently the opening times for the Helpline are from 06:00 to 23:00 on Monday to Saturday and 07:00 to 17:00 on Sunday and

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Bank Holidays. Post Office monitors the number of calls made to the Helpline.

9.6 Statistics available for the period from April 2011 to March 2014 show that:

Calls made: 1,825,059

Calls Answered: 1,687,537 (92.46%)

Average waiting time until answer: 45 seconds

Calls abandoned: 137,522 (7.54%)

9.7 As can be seen from the above calls the average waiting time was just 45 seconds. Over 92% of all calls made to the Helpline were answered. Of the abandoned calls, this will include all abandoned calls and therefore will not solely be callers who have decided to abandon their call because they cannot get through to the Helpline (for example they may have resolved the issue themselves).

Unhelpful, script based responses

9.8 The Helpline does not use scripts. The operators, many of whom are very experienced with Horizon, listen to the query and then using 'categorisations' in Remedy (the contact management system) the Post Office Knowledge Base is accessed where there are articles relating to that category of call. The operatoradviser then selects the relevant article according to the issue raised by the caller and relays the information to them. If the Knowledge Base does not provide the relevant information there is a second tier of advisors that the enquiry can be escalated to.

Many calls were afforded "Low Priority"

9.9 There is no priority system in place for calls to the Helpline with the exception of matters relating to robbery or burglary.

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Whilst those calls are dealt with as a priority other calls are answered and dealt with in the order they are received.

9.10 In addition, if the Subpostmaster was not satisfied by the advice provided they could seek a higher level of support as described at paragraph 4.6 of the Part One Briefing.

Alleged contradictory advice

9.11 No evidence is presented in the Report to support the view that contradictory advice has been given by the Helpline.

General

9.12 All calls to the Helpline are recorded by the Helpline operators in the NBSC call logs. The logs describe briefly the nature of question and the answer given if appropriate. The Report states that there is insufficient evidence within the call logs that have been provided to them to conclude what advice was provided. However, Post Office considers that if calls were not being answered or addressed appropriately then either the matters would be escalated (which would be noted) or there would be repeated calls about the issue that the Subpostmaster was facing. There would be evidence that the advice had not resolved the problem or the Applicant was not happy with the advice. In the absence of this or other circumstantial evidence then Post Office would suggest that the calls had generally been resolved satisfactorily whilst accepting that there may have been individual calls where an Applicant was not content with the advice provided.

9.13 At paragraph 9.2 the Report states that a frequent comment by the Helpline was that matters would resolve themselves. It is likely that this was reference by the Helpline to a Transaction Correction being generated following a surplus or deficiency and that would resolve the issue.

9.14 Through its own investigation Post Office has found no evidence to support the allegations that Helpline would often merely

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comment that matters would resolve themselves or be dismissive of any enquiry. In addition to the initial advice from the Helpline, if matters could not be resolved they could be escalated to a higher level of support. Support could have been provided by Field Support Advisors or other managerial support if it had been requested. Post Office is not aware of any wider systemic problems where this support was not being provided.

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**Post Office's response to section 10 – Limitations in the
Transactional "Audit Trail"**

- 10.1 Section 10 of the Report considers what it generically refers to as "limitations in audit trails". The Report is concerned that Subpostmasters are not able to investigate the root cause of errors (even where they admit it is caused by their own or an in-branch error) due to a lack of access to necessary transaction data.
- 10.2 The Report considers three situations:
 - a. Data that is not available on the day of the transaction under investigation;
 - b. Data that is available but after 42 / 60 days is no longer available; and
 - c. Data that is not available after suspension.
- 10.3 In general, Post Office considers this section is premised on a misunderstanding of the nature of the information needed by branches to investigate losses.
- 10.4 If at the end of a day, a branch produces a cash declaration that shows a discrepancy, then the branch will have access to a range of reports on different products and transactions to investigate the possible causes for the discrepancy (including a complete line by line listing of all transactions that day). This also applies at the end of the trading period as a trading period is either 4 or 5 weeks (28 or 35 days) and the above reports and data have always been available in branch for a minimum of 42 days.
- 10.5 If a Transaction Correction is sent to the branch, the information needed to verify the Correction will not be the Horizon data (Post Office has this data and takes this into account when generating the Transaction Correction). The

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information is likely to be in the paper records held at the branch.

Data that is not available even from the day of transaction

10.6 Paragraphs 10.4 to 10.8 of the Report raise the issue that some information is not available to Subpostmasters even on the day that a transaction takes place. The example provided in the Report is where an aggregate amount or volume is provided for Debit or Credit Card transactions. An aggregate amount for the number of transactions was provided at the end of each day rather than a breakdown of the individual transactions. As a result, the Report states, that Subpostmasters are not able to identify the individual transaction that may have caused a balancing error. The Report considers that this would prevent a Subpostmaster from mitigating their loss or remedying the error by contacting the customer. This position was allegedly different prior to the introduction of Horizon when paper records were kept and could be reviewed.

10.7 Post Office does not understand this line of enquiry. Debit and credit card information has never been retained on Horizon in branch - indeed doing so would be a breach of Payment Card Industry standards (and Horizon is PCI accredited). However, as mentioned above, branches have always had access to line by line transaction data each day and this data records the method of payment (eg. cash, cheque or card).

Data that is available but after 42 days is no longer available (this was extended to 60 days)

10.8 On the original Horizon system, line by line transaction data was available in branch for 42 days after a transaction occurred. On Horizon Online (since 2010), this data is available for 60 days.

10.9 The Report considers that with data only being available for a limited period of time, it may not be available to support a challenge by a Subpostmaster to a Transaction Correction that

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may be issued after the date that data can be retrieved (ie. beyond 42 or 60 days). The Report states that this restricts Subpostmasters' ability to challenge Transaction Corrections.

10.10 What the Report does not take into consideration is that Subpostmasters may challenge a Transaction Correction without transaction data. Also Transaction Corrections are often preceded by an enquiry and so even if the Transaction Correction is beyond 42/60 days then an enquiry may well have been received within the period enabling the matter to be investigated within the 42/60 day period. There is a wide range of evidence that can be provided to review or challenge a Transaction Correction. Often it is very product specific and not a general view across all data entries. Typically, the necessary data is kept in branch records rather than on Horizon. These documents should be retained beyond the period that data is available through Horizon and is used by Subpostmasters to challenge or review a Transaction Correction.

10.11 For example, if a branch wishes to contest a Transaction Correction relating to ATM transactions (see section 5 above), the information needed is on the paper "Totals Receipt" printed daily by the ATM which shows how much cash has been dispensed by the ATM and other important information. This receipt must be retained in branch. No access to Horizon data is needed as all the necessary information is on the "Totals Receipt".

10.12 The general proposition in the Report that Horizon data needs to be available for more than 42 or 60 days is incorrect. Any challenge to a Transaction Correction, and the data needed to make that challenge, must be considered on a product by product basis. Post Office is prepared to investigate any product specific allegation that there is insufficient data or information available to Subpostmasters to challenge and review Transaction Corrections. It is confident that it will be able to show that sufficient information is available to Subpostmasters.

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Data that is not available after suspension

10.13 Paragraph 10.10 of the Report highlights that some Applicants were refused access to data following their suspension and access to their own records that may have been seized upon audit. As a result they say that they were unable to defend themselves from any claim made by Post Office for the recovery of monies.

10.14 Whilst Post Office are aware that some Applicants have raised the issue that their own records were removed and not returned to them there is no evidence produced or referenced by the Report to support the position that data being withheld has prejudiced an Applicant in any way.

10.15 As to other branch records, these are the property of Post Office. In the event of a Subpostmaster being suspended, Post Office may take away some branch records for investigation.

Giro Transactions

10.16 A connected issue that is considered at paragraph 17.4 of the Report is the process relating to Giro Transactions (under the heading counter errors that benefit customers). Giro Transactions are, in essence, deposits of cash into a customer's bank account. Previously, this involved a two-part paying in slip with one copy retained by the customer and the other retained by the branch. At the end of the day, the branch copy could be cross-referenced to the entry made on Horizon to check for any errors by the branch in keying in the wrong figure into Horizon. This process changed to a chip and pin system using a swipe card at the request of the processing bank (Santander) that ran the Giro banking service. Following the change, no deposit slip would be presented by the customer and no paper documentation was retained by the branch.

10.17 The Report states that due to the change in this process there is nothing to allow the Subpostmaster to check whether or not the cash deposit entries on the system reflected the amount of

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cash deposited. This is incorrect as the amount recorded on Horizon to be deposited is now confirmed by the customer through the chip and pin machine in branch. This is the same process used by all high street banks which have also moved away from paying in slips to card based deposits.

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**Post Office's response to section 11 – Transactions not entered by
Subpostmaster of their Staff**

11.1 Section 11 of the Report considers transactions that have not been entered by the Subpostmaster or their staff such as where there is an "automated transactional reversal". This appears to be the same underlying issue as raised in section 12 – see that section for Post Office's reply.

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Post Office's response to section 12 – Transaction Reversals

- 12.1 Section 12 of the Report considers the issue of Transaction Reversals.
- 12.2 Transaction Reversals are where part of a basket of transactions is reversed because the basket is interrupted before completion (typically due to a power or communication failure).
- 12.3 The Report states that when a Transaction Reversal happens, Horizon records the reversal against a user ID of the Subpostmaster or a member of staff. The Report states that this is misleading because the reversal is "automatic". This interpretation is incorrect.
- 12.4 As far as Post Office is aware, this issue has only been raised as part of a Spot Review conducted by Second Sight whilst preparing its Interim Report. The Subpostmaster who put forward the Spot Review has decided not to make an Application to the Scheme and no other Applicant has raised this issue.
- 12.5 As detailed in Post Office's response to the Spot Review (full details of which are confidential in order to protect the privacy of the Subpostmaster whom it concerned), the reversals were caused by the Subpostmaster cancelling a number of transactions that they were conducting for a customer. The user's System ID is shown as the person making the reversal because they initiated the reversal process.
- 12.6 The extracts taken from the report by Helen Rose (as quoted at paragraph 12.3 and 12.4) are taken out of context. The report was addressing concerns that reversals were not being clearly shown on the particular data being reviewed (ie. the ARQ and credence data being the main transaction data used by Post Office). However, this data is available on other records that can be extracted from Horizon. The report makes clear that this is not an issue with Horizon itself or its data but the way that

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the data it produced was presented within one particular data log. It does not suggest that there was any entry being made that was not initiated within the branch by the Subpostmaster or their staff.

12.7 This section raises no issue that could be the cause of losses in a branch.

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**Post Office's response to section 13 – Cash and Stock Remittances
(Rems) in and out of the branch**

- 13.1 Section 13 of the Report focuses on the remittance of cash and stock to and from branches. Paragraphs 7.16 and 7.29 of the Part One Briefing describe the remittance process.
- 13.2 On occasions issues can arise such as cash pouches not being received or there being less or more cash within the pouch than stated. This will result in a Transaction Correction being raised.
- 13.3 If the cash centre remits a cash pouch to a branch and it is not received this will not result in a loss to the branch. The cash centre will investigate why the pouch has not arrived and ultimately bear the loss. The cash pouch is scanned upon receipt by the branch and therefore it is only at this stage that the cash is registered on Horizon as being held in branch. From this point any loss of cash is the responsibility of the branch and Subpostmaster. There may be some occasions when the pouch barcode will not scan. In such circumstances the pouch is entered as received manually by keying in the barcode number.
- 13.4 If there is more cash within the pouch than stated the branch should report this within 24 hours of receipt. This will result in a surplus to the branch and a Transaction Correction is issued to correct the balance on Horizon.
- 13.5 In circumstances where the pouch contains less cash than expected the matter should be reported by the Subpostmaster within 24 hours of receipt. The issue is investigated by the Post Office cash centre. If the cash centre accepts that the pouch contains less cash due to their error they will bear the loss (if any). A Transaction Correction is issued to the branch to correct the balance on Horizon.
- 13.6 Where the cash centre does not accept that it is their error the Subpostmaster is invited to review the security cameras that

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monitor the loading of cash into the pouch at the cash centre. If the Subpostmaster wishes to continue to challenge the amount received they can do so through the FSC in the same way that a Transaction Correction is challenged. If less cash is held on Horizon a Transaction Correction would be issued. The loss can be placed in the suspense account whilst the matter is investigated and resolved.

- 13.7 A similar process is applied when cash is remitted to the cash centre from the branch. The amount of cash sent within the pouch is recorded. If this sum is more or less than anticipated when received by the cash centre the issue is investigated. The Subpostmaster has the opportunity to view security cameras that monitor the movement of the pouch and can choose to accept the shortfall / surplus or place the loss / gain into the suspense account and investigate the matter further.
- 13.8 Paragraph 13.4 deals specifically with the instances where foreign currency has been accidentally sent to the wrong branch. The Report speculates that this could result in a Subpostmaster being responsible for a delivery that was never received.
- 13.9 The same process outlined above applies to foreign currency. If a pouch is not received by a branch it will not be scanned into Horizon and there will be no increase in cash holdings. If the pouch is not received there is no loss to the branch.
- 13.10 Where the pouch is taken to a different branch in error it can be rejected and will be returned to the cash centre. If an alternative branch accepts the pouch it will be scanned into Horizon and increase the foreign current held at that branch. Transactions Correction will be issued to correct any discrepancies that may have been created but overall there would be no loss to either the branch that received the foreign currency or the branch that accepted it.

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Post Office's response to section 14 – Cheques

- 14.1 Section 14 of the Report discusses the process of remitting cheques from Post Office branches to Post Office's cheque processing provider. It considers the situations where cheques go missing and do not reach the cheque processor, or cannot be processed by the customer's bank.
- 14.2 To assist Applicants, Post Office has set out below the cheque remittance process and the process followed when cheques go missing or bounce.
- 14.3 In summary, it is inevitable that cheques will occasionally go missing at some stage in their processing. However, as stated in paragraph 14.6, provided that the Subpostmaster follows the correct procedure for processing the cheques in branch this will not result in a loss. The cost of a lost or bounced cheque is only passed to a Subpostmaster where there is clear evidence that the Subpostmaster has failed to follow proper acceptance or remittance processes and Post Office has exhausted all other possibilities of recovering the missing cheque. This is done in accordance with clause 12, section 12 of the Contract under which the Subpostmaster is liable for any losses caused by carelessness, negligence or error.

Process in branch

- 14.4 Most Post Office branches are entitled to accept cheques from customers as the method of payment for range of designated transactions. The cheque should be scrutinised by branch staff to make sure it is not a forgery and the reverse of the cheque needs to be date stamped, initialled and the relevant transaction details recorded. This will enable identification of the specific product and/or customer in the event of an error. There may be no customer details recorded on Horizon

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against the cheque transaction hence the need to endorse the cheque with those details.

- 14.5 The method of payment (**MOP**) by way of cheque should be recorded on Horizon. When recording a MOP as by cheque, the customer's cheque is automatically recorded on Horizon as a part of the branch stock.
- 14.6 All cheques taken should be despatched from the branch via the final Royal Mail collection of the day (except Fridays). The branch process for remitting cheques is as follows:
 - a. Subpostmaster produces a cheque listing report from Horizon (which shows the value of each cheque accepted that day).
 - b. Subpostmaster verifies that the cheques held in the till match (volume and value) against the cheque listing report.
 - c. The total cheque value is then marked on Horizon as being remitted to POL (known as "remmed out").
 - d. A further cheque listing report is then produced. This will show the cheques being remmed out as a negative value and the report will now total zero.
 - e. The cheque listing report is "cut off". The branch cheque stock will now also be zero.
 - f. A Batch Control Voucher (**BCV**) is manually completed to show number of cheques, value and despatching branch. The cheques are attached to the BCV. The cheques are then despatched for processing in the relevant envelope via Royal Mail to the cheque processor.
 - g. Horizon cheque listings and remittance slips are retained in branch.

FSC process

- 14.7 The POLSAP finance system at the FSC is automatically updated each night from Horizon (for the values of cheques remmed out

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from branches). The cheque team in FSC are able to view this data the day after the transactions and will see the outward remittances recorded.

- 14.8 Similarly an electronic file will be received overnight by FSC from the cheque processor via an automatic upload into POLSAP which shows the actual cheques received from each branch. FSC can then compare the values recorded by the branch as despatched against the values recorded by the cheque processor as received.
- 14.9 Approximately 1,000 entries will remain unmatched each day (ie. there is a discrepancy between the cheques received by the cheque processor and the information sent via Horizon by Subpostmasters about cheque remittances) and could be an indication of missing cheques. Many cases are resolved quickly (ie. late delivery by Royal Mail or the Subpostmaster missed the collection or forgot to put a cheque in a pouch). There will be around 100 cases per month where it becomes apparent that a cheque has actually gone "missing".

Investigating lost cheques

14.10 It is acknowledged that a cheque loss could occur at the branch, in the Royal Mail pipeline or at the cheque processor. Post Office's policy is that a branch will only bear the cost of a lost cheque if the branch has not followed proper procedures. If the root cause of a lost cheque is unknown or attributed to some other cause outside the branch, Post Office will absorb this loss and not pass it on to the Subpostmaster.

14.11 In the vast majority of cases, Post Office either mitigates the loss caused by a lost cheque or absorbs the loss itself. Only a very small number of missing cheque cases result in Transaction Corrections being issued to a branch.

14.12 The process for investigating missing cheques is as follows:

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- a. The transaction to which a missing cheque relates is (if possible) identified from the information input in to Horizon by the Subpostmaster.
- b. Branches will be contacted when the missing cheque case is set up to see if the cheque can be found in branch or if they are aware of which customer has presented the cheque which has subsequently gone missing.
- c. If the branch cannot find the lost cheque, a variety of techniques (depending on product/information available) are employed to identify the customer and their address from the transaction data.
- d. The customer is then contacted to request a replacement cheque. If a replacement cheque is provided then the loss to Post Office is avoided.
- e. If a replacement cheque is not forthcoming, the relevant client organisation (ie. the product supplier, say Bank of Ireland, Environment Agency, etc.) is informed that the payment for that particular transaction has not been received and the transaction is reversed where possible. By reversing the transaction the loss to Post Office is avoided.
- f. Alternatively, if Post Office is unable to identify the customer details, the relevant client organisation may be asked to try to contact the customer directly for payment. By payment being made direct from the customer to the client the loss to Post Office is avoided.
- g. If the transaction related to the missing cheque cannot be identified or if the transaction is identifiable but payment cannot be recovered from the customer or the client and the transaction cannot be reversed, Post Office will absorb the loss of the cheque provided discussions with the branch and review of transactional data does not reveal a breach of the operational processes.

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14.13 There are two typical scenarios where Subpostmaster has failed to follow operational processes and will be held liable for missing cheques:

- a. Cheques have been accepted by the Subpostmaster for a non-cheque acceptable product (e.g. foreign exchange sales). By accepting payment by cheque for a non-cheque acceptable product, it may not be possible to link a missing cheque to a transaction record. If the transaction record cannot be identified then it may not be possible to identify the customer and/or client. This then frustrates Post Office's usual loss mitigation steps described above.
- b. The method of payment has not been correctly recorded on Horizon with the cheque as the MOP and it subsequently proves impossible to associate any transactions with the missing cheque. Such an instance will typically be illustrated by branches recording multiple/all transactions through "Fast Cash" and then introducing a bulk cheque value to Horizon via a "Cash/Cheque Adjustment" at the end of the day prior to remitting out. Again, this may frustrate Post Office's usual loss mitigation steps described above.

14.14 Where a Subpostmaster is held liable for a missing cheque, a Transaction Correction will be sent to the branch reversing the remittance of the cheque by the branch. This will return the value of the "missing" cheque to the branch's cheque stock. If the branch cannot obtain a replacement cheque from the customer, there will be a cheque shortage at the end of the trading period that the Subpostmaster will need to make good.

Bounced cheques

14.15 Paragraph 14.4 makes reference to specific complaints by Applicants (rather than it being a common theme amongst Applicants) that they were liable for cheques that bounced. As described above, the branch accounts treat cheques like a stock item. So long as the branch accurately records the receipt of

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cheques from customers and the remittance of cheques to Post Office, then the branch is not concerned with the banking of any cheques. The banking of cheques and recovery of payment from customer's bank is conducted by FSC. Post Office absorbs the credit risk posed by accepting payment by cheque and should a cheque bounce, Post Office will absorb the resulting loss.

14.16 The only exception to this rule is where the branch has failed to follow operational procedures. This may have included not completing the details in accordance with a cheque guarantee card (until these ceased in 2011) or taking payment for a product where payment by cheque is not permitted.

Transaction Corrections for missing or bounced cheques

14.17 Paragraph 14.5 makes reference to Applicants not being able to mitigate their losses as the transaction correction for a missing or bounced cheque has been sent to them too long after they accepted the cheque. Transaction corrections may be delayed on occasions but this is not the fault of Post Office. In some instances Post Office is dependent on a response from a third party (such as the customer's bank) before the Transaction Correction can be issued. This may have resulted in some delay but, as stated above, if the correct process is followed then Subpostmasters will not be liable for any lost or bounced cheques.

14.18 Typically, however if there is an issue with a cheque this issue will be raised through other channels with the branch. In most cases, the branch will be aware of the issue long before the Transaction Correction is submitted.

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Post Office's response to section 15 – Pensions and Allowances

- 15.1 Section 15 of the Report concerns the risk of fraud taking place in relation to Pensions and Allowances (**P&A**) transactions. In particular the Report states that Subpostmasters could be innocent victims of this type of fraud but still liable for the resulting losses in their branches.
- 15.2 For the reasons set out below, P&A fraud by branch staff can be easily detected by a Subpostmaster before any loss occurs so long as he/she is carrying out proper end of day checks on P&A transactions. Subpostmasters are therefore liable for any losses in their branch caused by P&A fraud as this loss arises due to their failure to conduct adequate checks.

Benefit payment methods

- 15.3 There are various methods by which benefits can be received by customers:

P&A books

- 15.4 P&A books were provided by the Department of Work and Pensions (**DWP**) to customers entitled to benefits. A nominated Post Office branch was set out on the cover of each P&A book, together with the customer's name and address. Within each book were (usually) 20 dockets, vouchers or foils (referred to in this Reply as vouchers) stating the FAD code of the nominated Post Office branch, voucher number and amount to be paid. The vouchers were presented to the branch staff, processed through Horizon and then cash paid to the customer. The vouchers were despatched each week by each branch to the Paid Order Unit (which in effect is the DWP) in Lisahally, Northern Ireland.
- 15.5 P&A books ceased to be used in circa 2005 and were replaced with Post Office Card Account.

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Post Office Card Account (POCA)

15.6 POCA is a limited service bank account that only allows benefits to be deposited into the account by DWP and cash to be withdrawn. Withdrawals are conducted by the customer taking his POCA card into a Post Office and withdrawing in cash either some or all of the benefits within his account.

Green Giros

15.7 Customers who lose their POCA cards or customers who are on temporary benefits may be sent Green Giros by the DWP.

15.8 These are cheques (also known as DWP cheques) which set out the payment amount and can be cashed in the usual way. These cheques are date stamped and retained by the Post Office after paying the customer. They have historically been accounted for and despatched by each branch weekly to Alliance & Leicester. They are now sent to Santander (both banks are referred to in this note as Santander for ease of reference). Green Giros should not be confused with Giro Payments which are an entirely different product.

P&A fraud

15.9 P&A fraud encompasses a number of different types of fraud, some of which are historical due to the change in payment methods over time.

Overclaim fraud

15.10 For each benefit payment to a customer recorded on Horizon, the branch should take from the customer the associated P&A voucher or cheque and remit each week all vouchers to the DWP and all Green Giro cheques to Santander. An overclaim occurs when the branch records a benefit payment on Horizon but does not remit the associated voucher or cheque. Without the voucher / cheque POL cannot recover the payment from DWP / Santander. This places a loss on POL which is then passed to the branch by way of a Transaction Correction (formerly known as an error notice,

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but referred to in this note as a Transaction Correction for ease of reference).

15.11 Overclaims are relatively easy to identify as the branch must record the remittance of vouchers or cheques out of the branch on Horizon and therefore it is possible to identify any missing weekly remittance.

15.12 A fraud can be committed by recording fake benefit pay-outs on Horizon, which lowers the amount of cash recorded to be in the branch (as Horizon assumes the cash has been passed to the customer). This causes a short term surplus (until the missing voucher / cheque is discovered and a Transaction Correction sent through) which can be used to cover other losses or removed from the branch at the end of trading period (assuming that there are no other offsetting losses).

Reintroduction fraud

15.13 Reintroduction fraud is a more sophisticated version of overclaim fraud whereby the false benefit pay-outs are disguised by the submission of duplicate paperwork.

15.14 In reintroduction fraud, a legitimate benefit pay-out is recorded on Horizon with cash being paid to a customer but with the corresponding voucher / cheque not being date stamped or remitted out to DWP / Santander. At a later date (typically the following week), the same benefit pay-out is recorded again on Horizon. This time however no cash is paid to a customer (as the customer is not present) but the previous voucher / cheque is date-stamped at the later date and remitted to DWP / Santander.

15.15 For example, in week 1 there would appear to be an overclaim (amount claimed but no corresponding voucher or cheque). The amount would be claimed again in week 2 by submitting the cheque or voucher from week 1 (by this time date stamped). The fraud is premised on DWP / Santander not spotting the missing voucher or cheque in week 1 or the reintroduced voucher / cheque in week 2.

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However, in practice, each voucher / cheque has a unique reference number which allows duplicate paperwork to be identified.

15.16 Each of these frauds has taken place both before the introduction of Horizon and when Horizon was in operation in Post Office branches. This is not a Horizon related issue. It is also largely an historic issue as most benefit payments are now through POCAs (which are not susceptible to the above frauds) although some Green Giro Cheques are still processed in branches.

Fraud prevention in branch

15.17 It should be noted that "overclaims" and "reintroductions" will not cause a loss to a branch. They generate a cash surplus, which as long as the cash had not been removed from the branch, will off-set any later Transaction Correction.

15.18 It was historically and remains open to a Subpostmaster to carry out immediate checks for P&A fraud as a Subpostmaster will have access to (i) each week's batch of cheques/vouchers and (ii) that week's records of P&A transactions as recorded on Horizon. It is therefore possible for a Subpostmaster to easily confirm that the value of the cheques and vouchers being remitted each week match the value of benefit pay-outs recorded on Horizon. This would reveal any overclaims or reintroductions.

15.19 For this reason, Post Office does not consider that a Subpostmaster could be the innocent victim of P&A fraud. Although they may not have committed the fraud, they are easily able to prevent it. If a Subpostmaster does not follow the proper process for remitting out P&A documents, and thereby fails to stop any overclaims or reintroductions at source, they are liable for any resulting losses.

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Post Office's response to section 16 – Surpluses

- 16.1 Section 16 of the Report considers Post Office's approach towards the surpluses that may be generated within branch.
- 16.2 As stated at paragraph 16.1, the contract between Post Office and Subpostmasters allows surpluses to be withdrawn provided that any subsequent charge is made good immediately. This means that Subpostmasters may retain surpluses that may be generated. The report confirms, correctly, that Post Office views both surpluses and deficits as discrepancies. However, the Report makes the incorrect conclusion that Post Office are not as concerned with discrepancies as they are with deficits.
- 16.3 Whenever Post Office discovers a discrepancy that can be attributed to an error in branch, whether it is a surplus or a deficit, it will generate a Transaction Correction to correct the branch's accounts.
- 16.4 Where discrepancies occur in branch (say at the end of a trading period where there is a shortage or a surplus of stock or cash), it is for the Subpostmaster to dispute the discrepancy. This is done by contacting the NBSC. As there are more challenges to deficit discrepancies (and debit Transaction Corrections) Post Office spends more time investigating deficits than surpluses.
- 16.5 The system processes six million transactions every working day. Post Office only investigates a discrepancy in branch if the Subpostmaster requests assistance – it does not investigate every discrepancy identified in a branch's accounts:
 - a. First, most discrepancies are fairly small and so do not warrant a full investigation unless the Subpostmaster raises an issue.
 - b. Secondly, the sheer volume of discrepancies would make investigating them all unworkable.

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- c. Thirdly, where a discrepancy arises in branch (ie. the cash on hand does not match the cash figure on Horizon) an investigation will require close involvement of the Subpostmaster and their staff as only they will know how the branch has transacted its business.

16.6 The Report's conclusion that Post Office is not concerned with surpluses is therefore not correct. In any event, it is noted that this topic does not give rise to any thematic issue that indicates the Post Office or Horizon is responsible for losses caused in branches.

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Post Office's response to section 17 – Counter-errors that benefit customers at the expense of the Subpostmaster

- 17.1 Section 17 of the Report considers occasions when customers may benefit from certain errors in branch to the detriment of Subpostmasters. This section does not give rise to any thematic issue but rather appears to raise a series of discrete points.
- 17.2 Paragraph 17.1 of the Report highlights that mistakes can occur when a counter clerk presses the "Deposit" icon rather than the adjacent "withdrawal" icon. This error by a Subpostmaster or their staff would have the effect of doubling the size of the error (as the branch will record the receipt of money into the branch in the accounts which increases the recorded cash position but will have also handed over cash to the customer thereby lowering the amount of cash in the branch).
- 17.3 Post Office agrees that this error may occur but that this would be an error within the branch, not a systematic problem with Horizon. In these circumstances the Subpostmaster would be liable for the error and any loss that has been created in accordance with section 12, clause 12 of the Subpostmaster contract.
- 17.4 Paragraphs 17.2 and 17.3 are a repetition of the issue raised in section 19 – to which see Post Office's comments on that section.
- 17.5 Paragraphs 17.4 – 17.8 are a repetition of the issue raised at paragraph 10.1 – to which see Post Office's comments on that section.

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Post Office's response to section 18 – Error and fraud repellency

18.1 Section 18 of the Report considers whether Horizon is sufficiently error and fraud repellent. It raises 4 issues:

- a. Has Post Office sufficiently upgraded and developed Horizon over time?
- b. Does Horizon accurately record transactions processed in branches?
- c. Is Horizon resistant to power and telecommunications failures?
- d. Should Horizon work for every single user no matter their competence?

Developing Horizon

18.2 The Report states that Post Office has not sufficiently upgraded and developed Horizon over the years so that there is a situation where "*errors and fraud that could possibly have been designed out of the system*" did not happen. As a result, the Report alleges that Subpostmasters have been liable for losses that could have been avoided.

18.3 This conclusion is unsupported by any evidence and is incorrect.

18.4 The Report contains ~~has undertaken~~ no analysis of the development of Horizon over the years. It is unclear on what basis the Report considers Horizon to be under-developed when there has been no consideration of Post Office's processes for reviewing and improving Horizon or of the upgrades that have been implemented.

18.5 The Report references a single example to support its opinion:

"18.4. A good example is an issue that has been raised by Applicants in regard to Giro transactions. This relates to

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Horizon operating in Recovery Mode, for example following power or telecommunications failures that resulted in the branch terminals freezing. In these situations the system goes through a complete reboot, then, when it has finally rebooted, a message appears on screen asking "do you need to recover any Giro transactions?"

18.5. *A few Applicants have reported, when faced with that question, they usually did not have sufficient information to know whether or not the system needed to recover any Giro transactions. If they responded in the affirmative, the system asked for the details of the Giro transactions that needed to be recovered. As the user did not have the relevant details to hand (and could not access the data as Horizon was still completing its reboot process), they were forced into responding in the negative and hoping that was the correct response. This often resulted in the 'wrong' answer being entered and transaction errors being generated."*

18.6 It is noted that this example does not include any suggestion as to the improvement or upgrade that could have been implemented by Post Office to alleviate the above alleged issue. This example does not therefore support the conclusion reached in the Report.

18.7 Post Office in fact has a number of processes in place for regularly reviewing and improving Horizon. These include:

a. **Incident and Problem Management processes.** Both of these processes ensure that where a branch reports an issue it is investigated and resolved. Where several instances of the same issue occur, then a problem record is created and the root cause of the issue is identified and fixed (ie to avoid further instances). The resolution of problems can sometimes be minor amendments to processes or can result in a change to the software code via the next release of upgraded software.

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- b. **Operational reviews with Fujitsu.** These take place on a monthly basis across a number of different specialist teams in both Post Office and Fujitsu. The purpose is to monitor and review past performance, addressing any issues as required, and to prepare for known changes or upcoming events.
- c. **Operational reviews with the NFSP.** These have been in place for over 10 years and have operated on either a monthly or quarterly basis across this period. It has involved the NFSP Executives meeting with senior representatives from Post Office's IT Service, Network and FSC teams. A number of operational issues are raised via these meetings and actions taken to resolve and improve either Horizon or associated processes. Other systems are also discussed as and when relevant eg ATM's.
- d. **Continuous Service Improvement.** This is a standard process that Post Office's IT Services operates with all of its suppliers. Post Office considers that Fujitsu are particularly good in this area and have over a number of years developed and introduced a number of improvements. This has included Fujitsu, by their own initiative, providing additional funds to be used by the Post Office for improvements to Horizon. Fujitsu were not contractually obliged to do this. The approach agreed with Fujitsu was to use NFSP's input to drive the improvement initiatives. Through this process and the tri-party working, including NFSP members active involvement in conducting demonstrations and tests, resulted in improvements directly driven by the NFSP and funded by Fujitsu.

18.8 Ultimately, the Report appears to agree with Post Office's position in that it states at paragraph 18.8 that "*a number of enhancements have been made to Horizon following experience and feedback*". Whilst specific examples are not provided as

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evidence, this shows that Post Office is engaged in evolving its systems to improve user experience.

Accuracy of capturing transactions

18.9 At paragraph 18.9 the Report states that, in their opinion, for Horizon to be "*fit for purpose*" for all users it needs to record and process a wide range of products and services offered by Post Office and to enable Subpostmasters to investigate any cause of issues that may arise. The Report concludes that from the cases reviewed, although no specific examples are provided, that although the core software of the system works it may not provide an ideal user experience for less IT literate users.

18.10 Horizon is capable of capturing all information and processing all transactions if used properly. No system errors have been highlighted in the Report. Further, no examples or explanations are provided to suggest that Horizon, if operated in accordance with standard operating procedure, would not accurately capture transaction data.

18.11 In fact, of the cases that have been fully reviewed so far, not one has presented any evidence whatsoever that Horizon did not accurately record the transactions processed by Applicants or their staff.

18.12 Horizon is designed to ensure the accuracy of transaction data submitted from branches. Safeguards are in place to ensure that no transactions are lost, altered or improperly added to a branch's accounts:

- a. **Encryption.** Transmission of transaction data between Horizon terminals and the Post Office data centre is encrypted.
- b. **Net to Nil.** Baskets³ must net to nil before transmission. This means that the total value of the basket is nil and therefore the correct amount of payments, goods and

³ See paragraph 7.15 of the Part One Briefing for an explanation of "baskets".

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services has been transacted – as the value of goods and service should always balance with the payment (whether to or from the customer). Baskets that do not net to nil will be rejected by the Horizon terminal before transmission to the Post Office data centre.

- c. **No partial baskets.** Baskets of transactions are either recorded in full or discarded in full – no partial baskets can be recorded.
- d. **No missing baskets.** All baskets are given sequential numbers (called "Journal Sequence Numbers" or JSNs) when sent from a Horizon terminal. This allows Horizon to run a check for missing baskets by looking for missing JSNs (which triggers a recovery process) or additional baskets that would cause duplicate numbers (which would trigger an exception error report to Post Office / Fujitsu).
- e. **Secure data store.** Transaction data is stored on a secure audit server. All transaction data is digitally sealed – these seals would show evidence of tampering if anyone, either inadvertently, intentionally or maliciously, tried to change the data within a sealed record.

18.13 In summary, Post Office remains confident that Horizon accurately records transaction data and the Report presents no evidence to change this conclusion.

Power and telecommunications failures

18.14 Paragraph 18.10 says that for Horizon to be effective, the system must be able to operate in areas where power and telecommunications reliability is a problem. It is noted that the Report does not offer a view on whether Horizon achieves this standard.

18.15 For clarity, Post Office maintains that Horizon is capable of handling power and telecommunications problems.

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18.16 In Post Office branches, Subpostmasters are responsible for power supplies and the cabled telecommunications line (see paragraph 5.6 in the Part One Briefing Report). Interruptions in power supplies and telecommunication lines are a risk faced by all IT systems. There are however recovery systems built into Horizon to prevent losses occurring where there is a power or telecommunication failure. The following is a description of the recovery process:

- a. Following a failure to contact the Data Centre and complete a transaction, the system would automatically carry out a retry and attempt to save the basket to the Data Centre again.
- b. Following the failure of the second attempt, a message displays to the User informing them that there was a failure to contact the Data Centre and asking them if they wish to Retry or Cancel. It is recommended that Users only "Retry" a maximum of twice.
- c. When the User selects "Cancel" this results in a Forced Log Out. This means:
 - i. Horizon would cancel those transactions that could be cancelled.
 - ii. Horizon would then print out 3 copies of a Disconnected Session Receipt (one for the customer, one for branch records and one to attach to the till to aid with recovery).
 - iii. The receipt would show transactions that are either recovered or cancelled. Those products considered recoverable must be settled with the customer in accordance with the Disconnection Receipt.
 - iv. If a transaction is cancellable then stock should be retained by the branch.
 - v. Horizon would then log out the active user.

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- d. The Subpostmaster should then make sure that, in accordance with the Disconnect Receipt, the Customer is provided with any funds due to be returned to them in accordance with the Disconnect Receipt.
- e. The system would then display the Log On screen. The User may then attempt to Log On again.
- f. As part of the Log On process, the system checks the identity of the last basket successfully saved at the Data Centre and compares it with the identity of the last Basket successfully processed by the counter. If the last basket saved in the Data Centre has a higher number than that considered to be the last successful basket processed by the counter, the recovery process at the Counter would then repeat the process that the counter had carried out at the point of failure.
- g. A Recovery receipt would have been printed reflecting these transactions.
- h. A message is displayed to the user confirming that the recovery is complete. They then return to the Home screen. Depending on the transactions being conducted at the time, the user may be asked a series of questions to complete the recovery process.

18.17 It is noted that in Second Sight's Interim Report last year, it specifically looked into this recovery process following a telecommunications failure. Second Sight found that the recovery process worked but questioned the speed of the response from Horizon. As far as Post Office is aware, this conclusion is still valid and has not been revoked by Second Sight.

18.18 The Part Two Report states that there are cases where errors are more likely to occur when unusual sets of circumstances and behaviour are present. It is not clear what these circumstances or, in particular, the behaviour is and so Post Office cannot comment on this line of enquiry.

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Fitness for all users

18.19 At paragraph 18.11, the Report notes that there are some people who are unsuited from the outset to using a computerised branch. It is not understood how this relates to the question of whether Horizon is fit for purpose. However, in general, there is an effective recovery process to manage power and telecommunication failures.

18.20 Horizon is operated by thousands of Subpostmasters, the majority of whom have not had any issue with the system or the effectiveness of it. Whilst a small number may find the operation of the system difficult, this does not make Horizon not fit for purpose. The subjective experience of a few people is not evidence that an IT system is objectively not fit for purpose.

18.21 For this assessment to be carried out the Report would need to identify some form of industry benchmark against which to judge Horizon. Also, the phrase "fitness for purpose" has a specific legal meaning and is therefore a subject on which Second Sight has no expertise to offer an opinion. The Report does not establish or seek to articulate any ~~is exercise of establishing~~ a legal or industry benchmark ~~has not been undertaken~~ and so ~~the Report's~~ findings are entirely unsupported by evidence or any robust analysis.

18.22 Post Office maintains that the fact that over 450,000 users have used Horizon since its inception and only 150 have raised a complaint to the Scheme shows that it is fit for purpose.

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Post Office's response to section 19 – One-sided transactions

19.1 Section 19 of the Report comments on what it calls "one-sided transactions". These are transactions that the Report states have not fully completed all the constituent parts of the transaction. This is either because there has been a charge to the customer for goods or services but they do not receive the goods/service. Alternatively, a transaction is processed but the customer's bank account is not charged for the purchase.

~~19.2~~ The Report speculates that these situations could, somehow, give rise to a loss to a Subpostmaster. ~~despite the lack of evidence.~~

~~19.3~~19.2 ~~Post Office has asked for more details on this alleged scenario.~~ Thus far Post Office has not been presented with any evidence that there is a general issue with Horizon or Post Office's processes that could give rise to the above scenario.

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Safeguards

~~19.4~~19.3 The Report suggests at paragraph 19.2 that one cause for a "one sided transaction" is due to a telecommunications failure. Post Office accepts that telecommunications issues can give rise to "one-sided transactions". This is an inevitable risk of transacting business across the internet and affects all retailers and banks. Also like all retailers and banks, Horizon has recovery processes in place to rectify any "one sided transaction" errors. These safeguards are specific to particular products so it is not possible to explain them all in one document.

~~19.5~~19.4 Communication failures can have two broad impacts. The main impact would be the type of interruption that is addressed by recovery prompts that are referred to at paragraph 18.16 of this Reply.

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19.6 19.5 The other impact (which would affect the customer, not the Subpostmaster) would be where a debit card payment was interrupted after the bank had ring-fenced the customer funds for the payment but before the counter confirmed that the transaction was complete. This can lead to a situation where although there is no issue for the branch accounts, the customer is no longer able to draw down on funds in their bank account because they remain ring-fenced for the original attempted transaction. Banks have routine processes to clear down ring-fences within a couple of days or on an accelerated basis by specific enquiry. This would not affect branch accounts but could of course lead to customer complaints to their banks.

No risk to branches

19.7 19.6 From a branch's perspective no discrepancy will arise from a one-sided transaction as the branch accounts are based on the information received by Horizon and not on the information held by a third party client.

19.8 19.7 If a transaction is recorded as completed on Horizon, then the accounts will also have recorded a corresponding payment from the customer or the handing over of cash or stock to the customer.

19.9 19.8 If Horizon records the transaction as failed, then the transaction will not complete on Horizon and no payment, to or from the customer, will be recorded. Likewise, as Horizon records the transaction as failed, the branch staff should not hand over any cash or stock to a customer.

19.10 19.9 Regardless of whether the client's IT systems record a completed transaction or not, the effect of the above is that the branch accounts will be in balance. The fact that there may be a discrepancy between Horizon and the third party client's records does not, as described above, change the branch's accounting position.

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Branch awareness of this issue

19.1119.10 At paragraphs 19.3 – 19.6 the Report states that the only way a one-sided transaction would be discovered is if the customer was to notify the branch. The Report goes on to suggest that where the customer has benefited from the transaction (ie they have received goods which they did not pay for) they would not be aware or would not say anything. Therefore the Subpostmaster would only be aware of the error if the customer disclosed it.

19.1219.11 For the reasons stated above, this view is incorrect and, in any event, irrelevant as a branch will never be liable for an error caused by a "one sided transaction".

Conclusion

19.1319.12 In summary, whilst the Report has yet to prove that this is a thematic issue of general application, Post Office has demonstrated that a "one-sided transaction" cannot give rise to a loss to Subpostmasters.

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Post Office's response to section 20 – Hardware issues

- 20.1 Section 20 of the Report makes some general comments and observations about Horizon terminals and other associated branch hardware. However, the Report does not present any evidence to support its speculations nor does it clearly identify any issues that may be common to many Applicants within the Scheme.
- 20.2 Post Office accepts that hardware problems can arise and that equipment is replaced from time to time. However, this is very dependent on the circumstances of an individual case and does not give rise to a thematic issue.
- 20.3 Further, the Report does not attempt to undertake any form of statistical analysis or industry benchmarking. In this area, it would be common to see an assessment of "mean time between failures" as a way of judging performance.
- 20.4 In any event, as described at paragraph 18.6 of this Reply, there is a recovery process in place to manage hardware failures.
- 20.5 Paragraph 20.1 of the Report highlights that some Horizon equipment is more than 10 years old. Whilst this may be correct, there is nothing to show that the age of the equipment is a cause of any losses.
- 20.6 At paragraph 20.2 the Report states that there is little routine hardware maintenance. This is correct but equipment is replaced as and when needed and this is industry standard practice.
- 20.7 Paragraph 20.3 states that many Applicants believe that faulty equipment could be responsible for the losses suffered. This is not correct and no evidence has been put forward to support the view that hardware issues have caused losses in branches.

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Post Office's response to section 21 – Post Office Audit Procedures

21.1—The Report says at paragraph 21.1 that Applicants were not provided with copies of audit reports, although it does acknowledge, at paragraph 21.2, that Post Office's current practice is to provide each Subpostmaster with a copy of any audit report. However,

21.221.1 ~~In response Post Office says that~~ the practice of providing a copy of the audit report has always been in place.

21.321.2 Post Office is not aware of Applicants not being provided with copies of audit reports when requested however Post Office cannot categorically say that this has never happened in an individual case. Nevertheless, the lack of access to an audit report is not a cause of losses in a branch and would not exonerate a Subpostmaster from their contractual responsibility to make good losses caused in their branch that were revealed by an audit.

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Post Office's response to section 22 – Post Office Investigations

22.1 Paragraphs 22.1 to 22.8 of the Report provide Second Sight's opinion on the process that is undertaken by Post Office when it investigates criminal activity in branches.

22.2 This topic is outside the scope of the Scheme (which is to consider "Horizon and associated issues") and is also outside the scope of Second Sight's expertise. Second Sight, as forensic accountants and not criminal lawyers, are not qualified to comment on Post Office's prosecution processes.

22.3 This is highlighted by the statement in the Report that the focus of Post Office investigators is to secure an admission of false accounting and not to consider the root cause of any losses. As explained at paragraph 3.9 of this Reply, by falsifying the accounts (whether through the inflation of cash on hand or otherwise) Subpostmasters or their assistants prevent Post Office from being able to identify the transactions that may have caused discrepancies and losses. The first step in identifying a genuine error is to determine the day's on which the cash position in the accounts is different from the cash on hand. Where the cash on hand figure has been falsely stated, this is not possible.

22.4 The false accounting therefore hides any genuine errors from Post Office and a Subpostmaster. It hides it at the time the losses occur and it remains the case now that Post Office is not able to identify which transactions may have caused the losses. The Report is therefore entirely incorrect in its evaluation of how Post Office prosecutes dishonest false accounts.

22.5 Given that this is topic on which Second Sight can offer no expert opinion, this Reply does not comment on this section of the Report other than Post Office is refraining from commenting further save to confirm that it rejects all the Report's findings in this section it.