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Date: 26 September 2019

Director General: Mark Russell (UKGI)

Lead Official: Tom Aldred (UKGI), Beth White (BEIS)

Lead Official Telephone: GRODepartment for
Business, Energy
& Industrial Strategy

Recipient	To Note / Comment	To Approve / Decide
Permanent Secretary	X	
Kelly Tolhurst	X	

Post Office Limited (POL): Quarterly update**Summary**

1. This is a regular quarterly update on Post Office Limited (POL), and follows the previous update submitted on 13 June.

Timing

2. Regular quarterly update. This also provides background for your upcoming meetings with Nick Read (30 September and 17 October) and Tim Parker (date tbc).

Overview

1. The new CEO has arrived at an important moment for POL. While headline financial performance is good and with a positive outlook, financial controls need to improve and we are currently withholding funding pending information on investment spending. Meanwhile, the litigation case has exposed both historic weaknesses and an ongoing need for culture change throughout the business.

Legal

2. Sparrow' litigation. POL has been developing its strategy for mediation, including detailed work by its legal advisors to understand and verify the magnitude of potential claims. Separately, UKGI and BEIS are engaging with HMT to discuss preparations and clearance processes for a possible settlement. The final strategy will be contingent on two processes: the judgment of the 'Horizon' trial (no date confirmed, but expected in the next month) and the Court of Appeal's decision on whether POL can appeal the first 'Common Issues' verdict (an oral hearing is due on 12 November). Mediation is unlikely to start before December, but we may need to move quickly to obtain the necessary approvals. UKGI and BEIS comms have met POL to discuss comms around the Horizon judgment. Further advice will follow the judgment and appeal hearing.

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Governance

4. New CEO. Nick Read joined as CEO on 16 September, and you are meeting him on 30 September, and again with Kelly Tolhurst on 17 October. He was previously Chief Executive at Extra Energy (2018-19) and at Nisa (2014-2017). UKGI and BEIS met with Nick on 17 September and he attended his first Board on 23 September. He has publicly stated his intention to establish a clear vision for POL within 100 days (by Christmas), and to agree this both across the business and with its wide set of stakeholders. As part of this, we understand that Nick plans a series of 'roadshows' with staff and postmasters.
5. Bonuses. Following BEIS' earlier steer to consider future executive/bonuses policy, at the September Board, Remco proposed measures to provide greater discretion in future. These changes would not be operational for 19/20 STIP or LTIP performance periods because to do so would breach contractual entitlement and thus leave POL exposed to legal challenge. We are waiting formal proposals from the Remco.
6. Future of STIP and LTIP. We have also been working with Remco on revised measures for STIP and LTIP for FY 20/21 onwards. While EBITDAS has been effective in focusing management on the turnaround and restructuring, we think we should think about moving away it because it doesn't capture change spend very well or balance sheet efficiency. We have also proposed a change in the operational performance measures to include achieving improvements in areas that the Common Issues judgement highlighted. We are currently waiting a new proposal from Remco.
7. Executive team and succession planning. POL's senior leadership team is in a period of significant transition. 2019 has seen the departure of the Chief Executive, General Counsel, Chief Information Officer and HR Director. It is quite likely that Al Cameron will leave POL, having stepped up to interim CEO and now returned to his role as Chief Financial and Operating Officer. Nick Read may also want to restructure the leadership team and populate it with people who share his vision. We have pushed POL to develop its succession planning and the Board needs to revisit this regularly rather than as a one-off.
8. NEDs. Following a selection process, POL has identified three lead candidates for the two open roles (all women, one BAME) and we expect them to request shareholder approval shortly. We are hopeful that they will be in place for POL's next Board on 29 October, but to guard against the prospect of a double gap on the Board, we have agreed to extend the term of one of the outgoing NEDs (Tim Franklin) until both new NEDs have joined the Board.
9. New leadership at PO Insurance. POI have appointed Ed Dutton as CEO, replacing Rob Clarkson, with a remit to execute its growth strategy. Ed had



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previously been CEO of British Gas Insurance for 8 years. In addition, Tim Franklin has been appointed as POI Chairman.

10. Culture change. The litigation case has exposed historic failings in POL's dealings with postmasters and a degree of complacency in preparing for, and reacting to, an adverse judgment. At the UKGI Board, you indicated that you see the POL Board's attitude to 2019/20 bonuses as reflecting the same problem, and that culture change must become a primary focus for the senior leadership of POL and especially its Chair, Tim Parker. Encouragingly, POL's Board had a discussion on corporate culture at September's Board and UKGI's NED suggested they commission an 'organisational health check' to provide a clearer picture of the current situation.
11. Engagement with the Chair. You are due to meet with Tim Parker in October, to provide clear direction on BEIS's priorities. We would also expect to send a new Chair's letter in early 2020 to supersede that of January 2019. We would also recommend that you aim to meet with the Chair on a quarterly basis, in line with best practice across the UKGI portfolio.
12. Framework Document. POL is finalising a corporate restructuring for increased efficiency and to ensure a robust governance framework is in place. As part of this project we are revising POL's Articles of Association and establishing a Framework Document for the first time. This will provide clarity on our relationship, governance requirements and information-sharing arrangements. Agreement has taken longer than expected, with POL's engagement generally slow and unduly legalistic. A few outstanding issues remain, focusing on Shareholder reserved matters and applicability of HMG pay guidance, but following progress at the September Board, we hope to agree these shortly.
13. Compliance with pay guidelines. POL have now agreed to stop offering private medical insurance (PMI) to new joiners and to state within the Framework Document that they will comply with guidance on public sector pay and terms. This is a positive development as it had been a sticking point for several months. POL is not currently required to comply with the £95k cap on exit payments but have indicated that they would face significant problems if they were. These relate to long-serving employees are covered by pre-existing agreements with unions, as well as the remuneration of their most senior executives.
14. Shareholder meeting. UKGI and BEIS will hold a formal Shareholder meeting with POL on 24 October covering issues of both operational effectiveness and policy. While standard practice across the UKGI portfolio, this was a missing piece of POL's governance and holding them every six months been stipulated as a requirement within the new Framework Document.
15. Board review and Chair appraisal. POL completed a Board evaluation in January 2019. We have agreed with the SID to delay the next review until March 2020 to allow time for the new Board members to form a view on its



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effectiveness. It makes sense to carry out the Chair appraisal at the same time.
This will be led by the SID and you will be invited to share your thoughts on the
Chair's performance.

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Government Strategy and Spending Review

21. Long term policy work: The Post Office policy team are working with UKGI and POL to develop options to advise the Minister on the 16th October on the following areas:

- Funding, ownership and commercial sustainability: we are exploring the feasibility of and case for continuing a Government subsidy post 2021, taking account of POL's aspirations to become commercially sustainable whilst recognizing the need to maintain a footprint that reflects POL's social purpose balanced against fair agent pay.
- Sustainability of the network and workforce relations: we are exploring a range of options from reviewing network size, access criteria and definition of a branch to potential L&D and professional development support offers for postmasters (to complement POL's agent pay initiatives)
- Role of social purpose: we are undertaking a review of cross-government agendas that could link with POL's 'social purpose' including the cross-government loneliness agenda (DCMS) and community assets agenda (MHCLG). We are also considering the role of community branches and exploring ways in which the social purpose could be better defined and measured.
- Alignment of POL's activities with wider Government agendas: we will be undertaking further work to better understand opportunities linked to OGD digitization of services vs tailored support for vulnerable customers.

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POL Business Strategy

25. Agent Pay. POL is carrying out a Review of postmaster pay in light of an increase in resignations, difficulty in recruiting people to run a post office and significant parliamentary and media attention. POL is implementing some 'quick wins', increasing fixed remuneration by 10% for all community and hard-to-place branches and bringing forward increases for banking transactions. Plans for addressing more fundamental questions about the structure and level of postmaster pay will be brought to the Board in October, and officials are engaging with POL on this work. These issues will be a crucial part of the 5YP and the wider issue of how to improve POL's relationship with postmasters.

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27. Franchising. POL is continuing to franchise its Directly Managed Branches (DMBs). There are currently 151 DMBs and POL has exited 37 of the 69 DMBs they plan to franchise in this financial year. This ongoing programme has led to a reduction in losses from this part of the network but continues to create noise in affected communities, mainly due to misconceptions in the consultation process. POL is currently reviewing its communications around the consultation process to mitigate these misconceptions and are due to report on the outcomes of this review on 30 September.

28. The Minister and officials are broadly satisfied that common concerns about decreased accessibility, service level and quality in franchised locations -are addressed by POL on a case-by-case basis. We continue to work closely with POL to equip Minister Tolhurst to address concerns about specific cases. Customer satisfaction levels are typically high after franchising has taken place. Further, we also plan to engage with Citizens Advice who are currently carrying out research to better understand customer satisfaction and difference in quality of service between traditional DMBs and franchised DMBs. Whilst they are due to publish a report on their findings in January 2020, we plan to engage with their recommendations early and build this into our long term vision work, as appropriate.

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32. Cash logistics. POL undertook a strategic review into its cash logistics operations and presented findings at the July Board. It has decided against either a material acquisition or divestment in this area and will instead focus on optimising the current operation. It will look to develop its technology and explore commercial partnerships to reduce the cost of excess capacity in the market. POL is onboarding staff with relevant experience and creating a business case.

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Annex C: Network performance

Network update

s/n	Network Programme	Commentary
1	Franchising	POL plan to franchise 69 DMBs in 2019/20 and have exited 37 YTD. Franchising can be poorly received by unions and local stakeholders but once open, customers usually welcome better accessibility and opening hours providing by the franchised branch.
2	New branches	POL plans to open 220 new branches in 2019/20 (92 opened YTD), to meet under-served customer demand and, in certain areas, to spread concentrated demand across a wider area.
3	Outreaches	Outreaches are typically small, part-time branches using a village hall or a mobile van which enable services to be provided to communities which would not otherwise receive them. While Outreaches can represent the most appropriate provision in rural areas for continuity of service, we have some concerns about their rapid increase.
4	Hard to Place postmasters	Around 361 postmasters have expressed a wish to leave the network but cannot because, under current policy, POL is only allowed to pay compensation to departing postmasters when a replacement branch is available - otherwise communities will lose their post office.

Network Accessibility Performance

Criteria	Total Population within 3 miles	Total Population within 1 mile	Deprived Urban Population within 1 mile	Urban Population within 1 mile	Rural Population within 3 miles	Postcode Districts less than 95% Population within 6 miles
Target	99%	90%	99%	95%	95%	0
Performance	99.7%	92.7%	99.4%	98.2%	98.6	4*

*POL is working on restoring services in these Post Code Areas

Network coverage of SGEIs (Services of General Economic Interest)

	Category of Service	No. of branches required	No. branches where service is available
1	Processing social benefits and tax credit payments to the public	11,000	11,491
2	Processing of national identity and licensing scheme applications	11,500	Client contract dependent
3	Universal payment facilities for public utility services	11,500	11,625
4	Access to postal services	11,500	11,625



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5	Universal access to basic cash and banking facilities, especially for rural customers and those on social benefits	11,000	11,491
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