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Post Office Limited – Strictly Confidential

POST OFFICE LTD BOARD MEETING (Company Number 2154540)

Meeting to be held at 9am on 26 November 2014
in the Boardroom at 148 Old Street, London EC1V 9HQ

Members of the Board will be asked to declare any interest that could give rise to conflict in relation to any item on the agenda at the beginning of the item in question. All interests so disclosed will be recorded in the minutes of the Board. If the Chairman of the meeting deems it appropriate, the member shall absent himself or herself from all or part of the Board's discussion of the matter.

09.00	1	CEO report on Business Priorities	Paula Vennells
09.45	2	Business Transformation	David Ryan/Martin Edwards/Martin George/ Nick Kennett/Kevin Gilliland/Neil Hayward
11.00		BREAK	
11.15		Business Transformation	
12.15	3	Existing and Transformational Risks	Chris Aujard / David Ryan/Mark Davies
13.00		LUNCH	
13.30	4	Financial Performance Update	Chris Day
14.15	5	Update on the BoI / Post Office Long Term Contract, taking into consideration Projects Titan and Hawk	Nick Kennett
14.30	6	POMS go/no go decision including Grant Thornton risk assurance	Chis Aujard/Nick Kennett/Mark Davies, Associate Director, Grant Thornton
15.30		BREAK	
15.45	7	Updates from ARC, Remuneration Committee & Nominations Committee	Alasdair Marnoch Neil McCausland Alice Perkins
16.05	8	Minutes of Previous Meeting and matters arising Committee Minutes for noting Status report update	Alice Perkins
16.10	9	<u>Items for Noting</u> • IA Audit Action Status Report Summary • Significant Litigation Report • Health and Safety Report • Sealings • Update on State Aid Process	Alwen Lyons
16.20	10	Any other business Date of next meeting: 28 January 2015	Alwen Lyons
16.30		**CLOSE**	

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CEO's Report – November 2014

1. Introduction to this month's Board and overall strategic priorities

Key issues for discussion at this Board:

- Since the early summer, we have been developing a turnaround plan to secure the long-term commercial future of the Post Office. To achieve this, the Business Transformation programme was mobilised in June 2014 and targeted with finding £200m to £250m improvement in EBITDAS performance by 2019/20. At the September Board, we discussed our core commercial strategies to 'Win in Mails', by becoming the most convenient parcels retailed in the UK, and to establish the Post Office as the leading challenger in financial services. And we focussed at the last Board meeting on the underpinning capabilities and activities required to reshape the business, and how we are managing change in our complex stakeholder landscape.
- Our *discussions at the November Board will bring the design work on the turnaround plan to its conclusion* and discuss the proposed next steps to put in place an orderly transition into implementation. The Business Transformation paper and associated material in the reading room represents a significant body of work and I hope the quality of the analysis gives you confidence in what we are undertaking, as well as a sense of the opportunities ahead as we shape our future.
- The paper builds on the Board's feedback on the initial Target Operating Model in September and *sets out the plan to transform the business* (the Roadmap), bringing together a number of significant in-flight programmes with new incremental initiatives. The Roadmap has sequenced the delivery of each programme to achieve, over time, a sustainably lower and increasingly variable cost base, and to deliver the required EBITDAS outcomes within an acceptable risk profile.
- Given the potential for significant changes in the business over the funding plan period (to 2017/18), we have defined *three strategic levers that we will use to adjust and recalibrate our plans* so we are well placed to respond to opportunities, risks and challenges as they arise. The levers are set out in more detail in the Business Transformation papers and accompanying appendix. These include working with other business partners (particularly recognising the critical dependency on our partnership with Royal Mail), adjusting our channel mix, and strategic portfolio management to ensure we are allocating our scarce capital to the areas of highest profitability and return on investment.
- There are significant risks in executing any turnaround programme, and that is the case for the Post Office. However, these risks should not deter us from action providing we are confident we have identified the relevant risks and have appropriate contingencies in place. The paper references *the analysis of risks to successful delivery and the associated mitigations*. The paper also draws on work undertaken by PwC to assure the assumptions underpinning the programme design and test the realism of the plan in the Post Office context. We have incorporated the recommendations into the Roadmap and the proposed transition activities, to ensure the organisation can subsequently embark on implementation with confidence.
- The paper summarises the conclusions of the design phase, and *seeks the Board's support to start the transition activities and to stand up the necessary programme governance and control framework*. Given the scale of the transformation activity, tight

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central control is proposed with integrated 'top down' governance. It is also proposed to return to the Board in Q4 2014/15 to confirm that sufficient progress has been made during the transition period, to then support the recommendation that implementation be progressed as an integrated portfolio of change from the start of the new financial year.

Assessing the overall implications for the business

- We have used a range of scenarios to model the financial sensitivity to changes in delivery of both cost out and revenue growth. At the top end of our central planning range – the scenario that we are targeting to deliver – breakeven would be achieved in 2016/17 (in line with our June awayday expectations) with a significant surplus by 2019/20 (in excess of the Strategic Plan target). At the bottom end of this range, breakeven would be achieved a year later in 2017/18. *Both these scenarios would represent a delay against the Strategic Plan expectation that we would achieve breakeven in 2015/16*, but nonetheless would still mark an historic achievement in making the Post Office profitable, in spite of the very challenging trading conditions.
- The business transformation paper sets out how the Roadmap and glidepath have been recalibrated to bring the funding requirements within the available envelope to 2017/18. However, *our capital position will remain heavily constrained throughout the plan period*, leaving limited scope for us to absorb new risks or priorities. Discretionary spending will therefore have to be very tightly controlled throughout the period. This will require us to be ruthless in our prioritisation of activity and allocation – and de-allocation – of resources.
- There is no doubt that delivering the Transformation Roadmap is a major undertaking for the Post Office and presents significant risks. However, it should be remembered that the *'do nothing' option is itself not without risk* – on the contrary, given the market and fiscal environment it is almost certain to end with the Post Office no longer being viable in its current form, potentially forcing a more difficult restructuring. The judgement for us is therefore about the robustness of the approach to managing and mitigating the inevitable risks and challenges we will face over the coming months and years. The analysis we have undertaken on strategic levers also means we are now well placed to take advantage of opportunities to develop the business further in future.
- Finally, delivering the transformation will require significant changes to our culture. We discussed this at the Board in October, and the People and Engagement Plan already includes actions to embed a more commercial and customer-focussed culture, and to develop our relationships with both the trade unions and the NFSP. We are now considering how we develop a more agile and streamlined business and I have asked Neil to factor this into his work on organisational design and development.

2. Commercial and business performance overview

Overall performance

- As the CFO's Performance Report sets out, trading remained disappointing in October. Operating profit in the month was £5.5m (£4.8m adverse the budget) bringing the year to date operating profit to £29.0m, and increasing the year to date shortfall versus budget to £23.4m.

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- Net income was £6.7m behind budget within the month and flat with last year. The budget shortfalls were in mails and retail, and in telecoms. Year to date, the net income shortfall was £31.5m, with two thirds of this attributed to mails and retail. Financial Services remains the only pillar tracking ahead of target over the year to date (with income 5.7% over the year to date compared with the same period last year).

Mails initiatives

- Whilst trading in the mails market remains fiercely competitive, in period 7 we did exceed our performance for the same period last year and we will need to continue to perform at this level during the vital Christmas period if we are to hit the revised forecast of £345m at year end. This uplift in performance has been mainly driven by the Sales Efficiency campaign in the agency network which completed training of 3,000 branches at the end of October. The average branch weekly uplift is currently running at 6.5% against a revised target of 6.4% and the project remains on target to deliver an incremental £3.5m of mails income. Delivery of our revised mails forecast is still dependent on Christmas trading delivering at least £2m more income than for the same period last year.
- As you know, last Sunday we launched the new Post Office Christmas marketing campaign, marking a return to TV advertising at Christmas after a gap of 5 years. The TV adverts are part of a wider campaign including: digital outdoor; in branch activity; online search and display; and an extensive social media campaign utilising additional celebrity content which also went live on Sunday.
- Initial reaction has been very favourable with the campaign receiving 14 online and offline marketing trade and business press mentions to date. We sent 1.3m emails to our customers on Saturday/Sunday morning inviting them to be the first to view the advert, with an average 27% open rate leading to 23,200 clicks to You Tube with 15k viewing the TV ad before it went live. The X Factor Ad on Sunday reached a minimum of 9m adults and we saw a 17% year-on-year increase in visits to www.postoffice.co.uk after the advert aired. So far on social media we have delivered 4.96 million impressions of the Xmas ad copy via Facebook and Twitter, generating 31.6k additional views of the TV advert.

FS initiatives

- Mortgage sales performance gained momentum in October. Run rates are still below our plan but we remain on target for the year-end given over-performance earlier in the year. Several new offers have been launched in order to be in a good place when we go into the final quarter.
- Moneygram and banking and payments services continue to perform well. The Post Office received very positive publicity on the back of Lloyds' recent announcement to close part of its branch network, with Vince Cable endorsing the important role we play in particular to ensure banking and payment facilities are available to vulnerable customers, and isolated, rural communities. We are leveraging this publicity by raising awareness of our banking services in branch, with the service already available to 95% of UK current account holders and discussions underway to increase this further. I have also now written to Vince Cable to take him up on his offer to convene a roundtable for us with the banks as we develop our banking services further, recognising that any development of the service must be commercially sustainable and in line with our business strategy to reduce calls on public subsidy.

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- Updates on Project Titan (travel insurance) and Project Hawk (delivering the insurance buy-out option) are provided in section 3 and the related Board papers on our long-term contract with the Bank of Ireland and POMS.

In-year cost reductions

- The in-year delivery of cost savings remains a top priority with our focus on delivering a year-on-year improvement in our underlying EBITDAS performance by March 2015. We are now on track to deliver over £50m of savings against our target of £60m, and intensive work continues to close the gap including tight controls on staff and project costs. More details are provided in the business transformation paper.
- As discussed at the last Board meeting, we have been developing a first wave of headcount reductions to deliver around £15m of savings in 2014/15, and consultation with staff will commence on the 24th November. The design for the second wave of staff changes will commence in December, and should be complete and ready for consultation from March onwards as Wave 1 completes. As we have discussed, delivering this scale of change is likely to require compulsory redundancies and conversations with the unions are well underway on this basis. We have also invested significant management time in communicating with affected staff to ensure the case for change is understood. Very positively, Unite (the largest union in the UK) has signed an agreement which secures co-operation on Business Transformation – including compulsory redundancy at 90 days if necessary – and a review of union Facility Time as flagged last month in the IR Strategy paper.
- Discussions with CWU on Supply Chain and Admin pay have continued to be challenging and the ballot for strike action resulted in a clear Yes vote. However, the result was significantly lower than in previous ballots in terms of both the majority and the turnout, reflecting the intensive investment in communication with staff over recent weeks. We are continuing to engage with the CWU, have offered to use Acas to resolve the dispute, and have contingency plans for strike action in hand. A further update will be provided verbally at the Board – at time of writing, no strike action has been called.
- To secure savings from our non-staff costs, we held a Town Hall event on the 6th November with our top 48 suppliers by spend. The event provided an opportunity to outline to our suppliers the long-term vision for the Post Office, set out our financial imperative to reduce costs and change ways of working, and to communicate a short-term ask to negotiate on current terms and a longer-term ask for expertise and ideas to save money and introduce new ways of working.
- Feedback from the event has been very positive, with suppliers keen to work with us and suggest ideas and new ways of working. Information is currently being collated and will be used to inform re-negotiations, which we anticipate will yield £10-£15m of cost savings. We are also reviewing how we support our procurement team to ensure they can act with confidence in progressing more radical ideas to save money for the business.

3. Update on key change programmes

We have started to transition to the new roadmap, with some additional programmes now reporting through to the Transformation Committee. This is in order to ensure clear, integrated governance of all Transformational change activity.

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a) Crown Transformation Programme

Status overview: The programme continues to deliver in line with targets across branch transformations, training (over 3000 staff trained), staff cost reductions (>470 FTE), SSK rollout (>480 rolled out), mergers and relocations. However the current P&L run rate at the year-end is forecasting a £2m loss primarily due to a £7m income shortfall. Overall customer satisfaction and queue time satisfaction are meeting (or very close to) the target.

Programme KPIs:	YTD			2014/15 FY	
	Target	Actual	Period	Target	Forecast
P&L run rate	-£14.4m	-£15.4m	Q1	£0m	-£2m
Number of branches transformed	275	278	P7	292	300
Number of branches franchised	41	30	P7	70	51-57
Customer satisfaction in transformed branches	85%	83%	P6	85%	85%
Queue time satisfaction	85%	85%	P6	85%	85%

Key milestones ahead:

Milestone	Target date	Current status
All retained branches transformed	By end March 15	On schedule (currently ahead of plan)
57 franchises live	By end June 15	Will be missed (minimum 13 will not be franchised under CTP)
518 Self Service Kiosks rolled out	By end Nov 14	On schedule

b) Network Transformation Programme

Status overview: The programme remains ahead of target on both contracts and openings. Transitional locals are progressing without significant adverse stakeholder reaction although the workstream is time-consuming as decisions need to be made on a case by case basis. The value for Money workstream has identified potential cost savings that will be investigated further by the Business Transformation programme. Discussions on the cliff are starting with the NFSP and co-ordinated via the P&E team.

Programme KPIs	YTD (P7)		2014/15 FY	
	Target	Actual	Target	Forecast
Contract signed (cumulative)	3,944	4,332	4,800	4,800
Branches Open (cumulative)	3,054	3,353	3,708	3,708
Customer Satisfaction (all branches)	90%	97%	90%	96%
Average increase in opening hours	40%	68%	40%	66%
Cost reduction (in-year cumulative)	482.2k	852.9k	2,500k	3,460k

Key milestones ahead:

Milestone	Target date	Current status
4,800 contracts signed	End March 15	At risk, but mitigations in place
3,700 converted branches open	End March 15	On schedule (currently ahead of plan)
Complete first evaluation of guided leavers process	End Sept 14	Complete
Start cliff preparation work	End Oct 14	Discussions started

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c) 'Win in Mails'

Status overview:

The Ivy pilots continue to roll out but usage remains extremely low. Digital marketing has been implemented and a range of other marketing and PR activities are underway to drive up Home Shopping Returns volumes.

The greatest challenge for the programme remains securing support from Royal Mail at the required pace. As the Board is aware, there was a Chair-to-Chair meeting between RMG and POL to secure this support where two shared workstreams were agreed: firstly, to map out the costs savings for both organisations from customer journey simplification; and secondly, a joint commitment to secure a network with a major retailer such as McColls.

On the first workstream, agreement has been reached between POL and RMG on the specifics of what needs to be delivered to support the extended trials, namely product simplification (to allow removal of weighing scales), changes to operational requirements (no segregation of parcels and RMG collections at the new sites) and requirements for the technical solution. Work is progressing to understand where there is potential to remove costs from both organisations – on the basis of simplification and changes to operational process.

To the second workstream, the commercials for an interim deal with McColls remain to be agreed and are expected to conclude by the end of November. However, this step is critical as it will crystallise the cost implications of the above changes for both businesses, upon which the operational agreements are dependent. Following commercial agreement, we expect to secure an MOU with McColls by mid-December.

Programme KPIs	**End October**		**2014/15 FY**	
	Target	**Actual**	**Target**	**Forecast**
New access points	135	152	400	400
Average transaction volume per site	5p/w (in 2014)	0.03	tbc	tbc

Key milestones ahead:

Milestone	**Target date**	**Current status**
135 access points live	End Sep 14	Completed
400 access points live	End Mar 15	At risk pending outcome of RMG discussions
Technical solution agreed with PO and RMG	Oct 14	Completed
RMG interim commercial agreement	Mid Nov 14	At risk
First strategic partner signed	End Dec 14	At risk
RMG agreement on final solution and commercials	End Mar 15	At risk
Rollout to first strategic partner	April 15	At risk
5 strategic partners signed	April 15	At risk

d) Business Transformation

Status overview: the design phase will be complete by the end of November having delivered an 'end state' operating model design and transformation 'blueprint'. Transition business cases are now being prepared to manage the transition from a 'design' to a

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'delivery' structure and operational efficiency accelerators. Final recommendations will be made to the Board in November to secure approval for transition into delivery.

Programme KPIs	YTD (week 33)		2014/15 full year	
	Target	Actual	Target	Validated
Delivery of in-year savings	£26.3m	£16.4m	£60.0m	£53.4m

Design Phase Key milestones ahead:

Milestone	Target date	Current status
Current state assessment complete	End July 14	Complete
Draft Target Operating Model	End Sep 14	Complete
Complete Transformation Blueprint	End Nov 14	On schedule
End design phase	End Nov 14	On schedule

e) Separation

Status overview: The programme is delivering against the revised timeline within the MSA Extension Letter, with significant milestones approaching before the end of the calendar year for Contact Centres, and ebusiness and Networks by the end of the financial year. A key enabler for eBusiness separation has recently been achieved with customers requesting the www.postoffice.co.uk website now being served content and tools from Post Office rather than Royal Mail. The majority of the business services have now been separated, with all the remaining IT ones planned to be separated by the end of quarter 2 2015.

Programme KPIs	YTD (P7)		Full programme	
	Target	Actual	Target	Forecast
Separation of IT systems	143	143	256	256
Separation of Business Services	120	120	131	131
Finance – headcount reduction	27.5	27.5	27.5	27.5

NB The team will also be monitoring the number of post-launch incidents for the newly separated systems such as Finance and HR.

Key milestones ahead:

Milestone	Target date	Current status
Facilities Management separation	1 Oct 14	Completed
Grapevine separation	1 Oct 14	Completed
eBusiness Release 5 live	End Jan 15	On schedule
HR Common Components separated	End Feb 15	On schedule
BT on boarding to ATOS helpdesk complete	End Feb 15	On schedule
Networks site migration end	End March 15	On schedule

f) IT transformation

Status overview: Fujitsu have informed Post Office that they are withdrawing from the Front Office procurement process. The programme has initiated a full impact assessment, with a specific focus on managing the risk around continuity of service. We have commenced discussions with Fujitsu to de-risk the Front Office execution by extending the contract beyond March 2017. Our initial view is that a 12 months extension is required; however we are testing this and looking at the commercial impact. The Board will have the opportunity to review the programme in January.

The updated Business Case shows an increase in transition costs and the programme is working with the finance team to minimise the exposure and to agree the most appropriate

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way to secure the funding. The increase is largely due to more informed bidder responses to the procurements and changes to assumptions in the original estimates for the Network tower. The latest costs and assumptions have been used in the Business Transformation Roadmap and financial glide path. Mobilisation of the EUC delivery team is underway following the award of contract.

Programme KPIs	YTD		Full programme	
	Target	Actual	Target	Forecast
Towers Contracts Awarded	1	1	5	5
3rd parties transitioned to Service Integrator (SI)	90	90	96	96
SI operating model processes accepted	23	20	23	23
Financial savings	£0	£0	£25m	£25m

Key milestones ahead:

Milestone	Target date	Current status
Mid term opportunities kicked off	End Nov 14	On track
B/O contract awarded	Paused pending alignment with Business Transformation	
F/O ISFT	End Feb 15	On track
Network ISFT	End Feb 15	On track
F/O Contract awarded	End June 15	On track
Network contract awarded	End May 15	On track
EUC service commences	End June 15	On track
PO IT fully separated	End June 15	On track

g) *People & Engagement*

Status overview: The People and Engagement strategy and detailed actions for the next 12-18 months have been agreed by ExCo and the Board. The actions within the plan are aligned to the accelerators and are underpinned by the business approach to risk management. Short term focus will be on: 1, Stakeholder management (inc. NFSP, TUs, RMG, BIS) 2,Supply Chain strike ballot closing on 18th November 3, Business Transformation Wave 1 activity and management OD

Key milestones ahead:

Milestone	Target date	Current status
Compelling narrative for change	Complete	Complete
Making it easy crowd sourcing in place	Complete	Complete
P&E toolkit in place for supporting change	Complete	Complete
See Union agreement for new collective framework	End Q3	On track
Finsbury Dials seen as Business Support Centre	End March 14	On track
New collective framework in place	End March 14	On track
New Union representative structure in place	End March 14	On track
NFSP new org in place	End Jan 15	On track
Serve notice on current IR framework	End Jan 15	On track
Existing IR framework ends	End April 15	On track
No of reps reduced from 41 to 20	End April 15	On track
Workshop delivered re managing change	End Dec 14	On track
Revised incentives & colleague offers in place	End March 15	On track
Revised perf management process in place	End March 15	On track
Sales capability plans agreed	End Jan 15	On track
Revised agent framework approved	End March 15	On track
200mail coaches in place	End Nov 14	On track
Completion of guiding coalition	End March 15	On track

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h) Titan

Status overview: this update reflects the whole programme but will move to Post Office only deliverables (rather than POMS) from December to ensure clear lines of governance. Contractual relationships with third parties for distribution and servicing are progressing slightly behind plan but the programme anticipates all will be completed within the required timescales. Key risks that PO board do not give authority to trade due to concerns over readiness, and FCA do not provide authorisation within required timescales. Contingency plans being developed for both to enable uninterrupted Travel Insurance sales. Costs and benefits forecast are in line with business case.

Programme KPIs	YTD (P7 cum.)		Full programme	
	Target	Actual	Target	Forecast
Contractual relationships in place	6	6	13	13
Systems in place	4	4	6	6
Staff in place	5	3	6	6

Key milestones ahead:

Milestone	Target date	Current status
Sign off of company formation	Complete	
FCA application submitted	Complete	
Web help contract signed	Complete	
Systems build complete	End Nov 14	On track
POL Board approve POMS plan	End Nov 14	On track
POL Board approve POMS to trade	Mid Dec 14	At risk
FCA authorisation received	Mid Dec 14	At risk
Initial trading (renewals)	End Dec 14	On track
Live for new business	End Dec 14	On track
Strategic system implemented	End Aug 15	On track

i) Hawk

Status overview: the Post Office and Bank of Ireland have agreed to appoint an Independent Expert (IE) to provide a valuation of the insurance business as there is significant variation between Post Office and Bank of Ireland valuations. FS will not be able to confirm if anticipated benefits are achievable until the IE valuation is received and there is a risk that the valuation may be higher than Post Office is prepared to pay. Support is being provided by both KPMG and Linklaters.

Milestone	Target date	Current status
Appoint Independent Expert (IE) with BoI	Start Dec 14	On track
Conclude IE valuation	Jan 15	On track
Seek PO Board approval to proceed	Feb 15	Contingent on valuation being in POL range
Sign transaction agreements	Mar 15	
Hawk Implementation programme	Dec 15	

j) Financial Services Investments and Savings Negotiations

Status overview: Negotiations with the Bank of Ireland continue with BoI IRRELEVANT IRRELEVANT The key points under discussion are: IRRELEVANT IRRELEVANT IRRELEVANT assessing an IRRELEVANT

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and IRRELEVANT FS are also waiting for the Bank of Ireland to respond on latest IRRELEVANT

Programme KPIs	2015/16	
	Target	Actual
Incremental increase in net Savings revenues	IRRELEVANT	0
Investments Negotiations		n/a

Key milestones ahead:

Milestone	Target date	Current status
Savings negotiation	End of Q3	On track
Investments negotiation	End of Q4	On track

k) Financial Services Sales Effectiveness

Status overview: This Programme has been set up to achieve break-even sales volumes in 2017/18 (10 sales per week per specialist as presented in the FS Strategy at the September Board) and then go on to deliver 15 sales per specialist per week by 2020.

Phase 1 of the "Post Office Money Academy" is due to go-live in support of broader Post Office Money sub-brand launch. Priority training modules are on track but LMS (Learning Management System) is still in design. We are working with L&D colleagues to launch with an interim solution.

Detailed KPIs are being developed.

Key milestones ahead:

Milestone	Target date	Current status
POM Academy Phase 1 launch	Start Jan 15	At risk
POM Academy Phase 2 launch	End Aug 15	On track
Salesforce Development Web leads	End Jan 15	On track
Salesforce Development release 3	End May 15	On track
Salesforce Development release 3.2	Mid Sept 15	On track
Technology for Frontline	Mid March 15	On track
Hub and Spoke	Mid Feb 15	On track
Data Enablement – Mortgage Income	End Nov 14	On track
Data enablement – PID approved	End Feb 15	On track
Data enablement – FAD codes	Mid June 15	On track

4. Market, political and external developments

- **Royal Mail interim results.** Royal Mail's CEO review put emphasis on the competitive environment and the reduction in the rate of growth of the addressable UK parcels market caused by the impact of Amazon's own delivery network. Media coverage picked up on Royal Mail's pleas for the universal service obligation to be revised and calls on Ofcom to speed up its review of direct delivery competition
    - Profit before transformation costs £279m. Positioned as an increase of £13m on an underlying basis with Group operating profit margin after transformation costs increasing by 70 basis points to 5.1%.

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  - Revenue growth of 2% to £4525m; Letters revenue increased by 1% with volume decline of 3%. Parcel revenue down 1% with volumes increasing by 2%. GLS (European operations) saw revenues and volumes up 7%. The CEO's review put emphasis on the competitive environment and the reduction in the rate of growth of the addressable UK parcels market caused by the impact of Amazon's own delivery network;
  - Costs up 1% - emphasis on tight future cost control in rest of the year.

- **Click and collect will rise in popularity as consumers look to keep costs down**. 95% of UK consumers plan to use click and collect this Christmas according to a Postcode Anywhere survey. Over two thirds cited the convenience of not having to wait in all day for a delivery and to avoid the cost of shipping. Almost 80% of online shoppers expected click and collect to be offered for free. Doddle, a third party collection point, announced it opened six new stores in early November, and has ambitions to open 300 collection points as part of its business plan. Meanwhile, Home Retail Group announced plans to close 25% of its 323 Homebase stores and focus on its Argos retail network. It recently refurbished its Argos stores in an attempt to adapt to the digital age and offers a collection point for eBay parcels.
- **Lloyd's Bank and Metro Bank provide update on profit**. Lloyd's Banking Group announced pre-tax profits of £1.6bn for the first nine months of 2014, down from £1.7bn for the corresponding period in 2013. Further to this, it announced it would close 150 branches and cut 9,000 jobs over the next three years. Halifax branches will be maintained. These jobs are likely to be replaced by its £1bn investment in digital products and services. Metro Bank reported narrower losses of £9.4m in 2014 Q3, an improvement on £9.9bn in Q2. Over a 12-month period Metro Bank has grown by 118%, driven by investment in infrastructure and technology.
- **Telecoms industry competition will heat up as incumbents expand product portfolios**. BT's mobile service is expected to launch in the first half of 2015. It has been suggested BT's mobile subscriber cost could be as little as £5 a month, lower than mobile subscriber costs of £14 to £20 at present for other providers. BT will benefit from combining domestic data, media and voice services with Wi-Fi and wireless roaming using the fixed-line and mobile assets it already controls. The launch of mobile services will also see BT offer quad-play bundles featuring mobile, fixed-line phone, broadband and television services, rivalling Virgin Media and Sky (triple-play). Vodafone will be launching home broadband and pay-TV services in spring 2015. Vittorio Colao, Chief Executive at Vodafone stated this was "more of a defensive, reactive move" and is a response to BT's own expansion plans. "We will follow whatever [BT] do and the level of aggressiveness in their pricing," added Mr Colao.
- **Virtual ID is coming to the UK**. Over 500,000 individuals are expected to begin using a government-backed virtual ID scheme, called Verify, which will prove a user's identity. Verify will allow personal data to be stored online and applications for driving licences and tax returns to be submitted digitally. Government said the new voluntary scheme means an identity card would not now be needed, since a person can prove who they are without one. People select one of five private providers under the Verify programme, including Post Office and Experian, to complete an online security check. Post Office is currently working closely with the Government Digital Service and our technical supplier, Digidentity, to ready our Verify service for launch in January 2015.

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Annex A: Forward Board meetings: overview of the sequencing of discussions on key business strategy issues

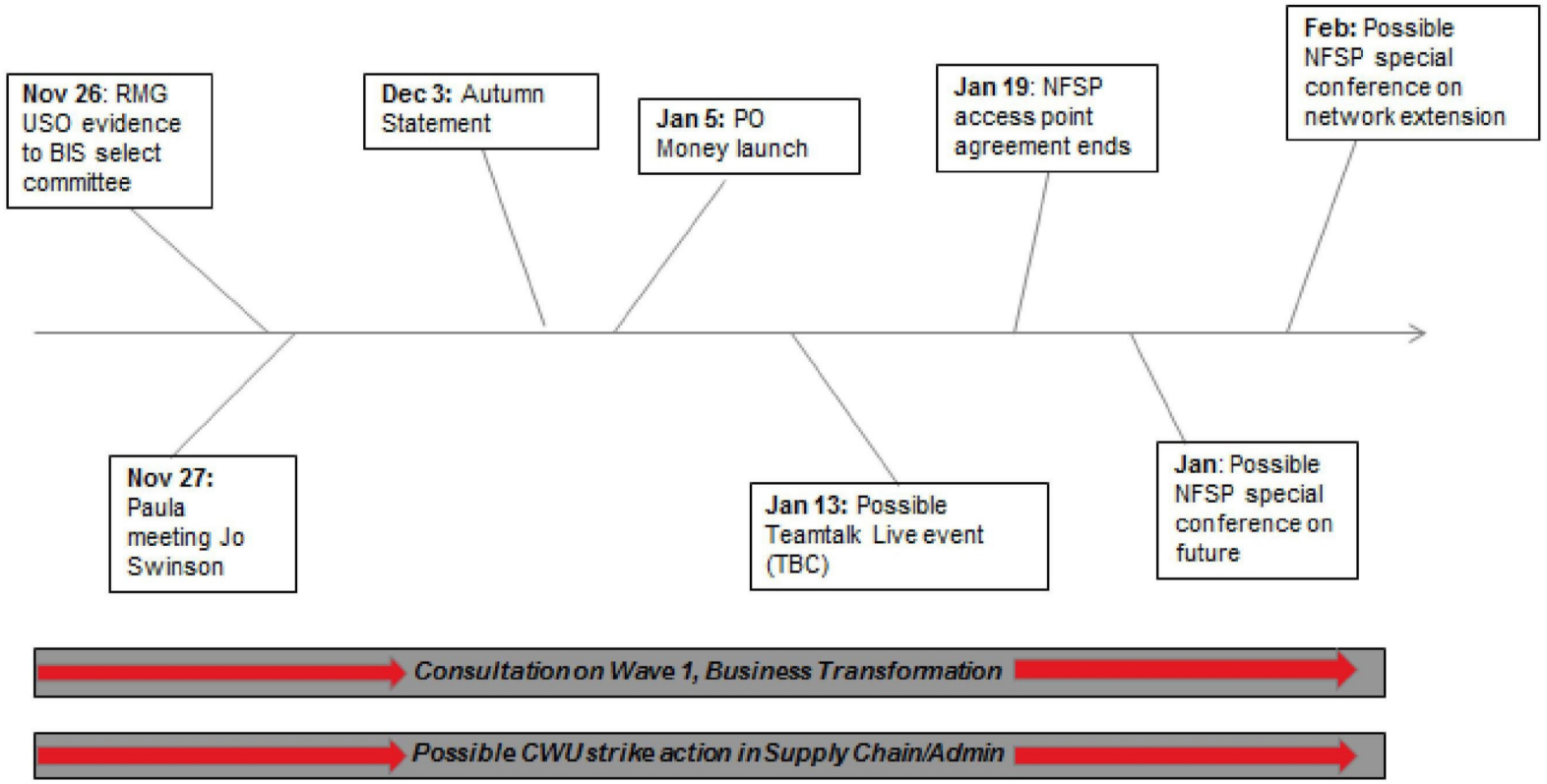
Key agenda items	Description
26th November:	
Business Transformation	Recommended TOM (informed by the September Board discussion) and the proposed roadmap to implement it. And outline the strategic levers to flex the plan to opportunities, challenges and risks as they arise.
POMs	POMs go/no go decision including Grant Thornton risk assurance
BOI/Post Office contract and relationship	Update on the BOI/Post Office Long Term contract, taking into consideration projects Titan and Hawk
28th January:	
Christmas trading and Mails	Report on Christmas trading Update on the Mails programme
Risk Appetite	Agree the risk appetite statements and risk rating scores as recommended by the ARC
Sales Capability	Progress update on work to build a world class sales capability – using all the levers to identify, source, develop, reward and incentivise the right sales behaviour.
Cyber Security	Lunch with Tony Smith from the Centre for Protection of National Infrastructure
SME & Digital	Progress update on development in SME and digital
IT including Fujitsu	Progress update on the IT strategy progress and the relationship with Fujitsu
25th March:	
1 year plan and budget	Approval of 1 year operating plan and budget
Scorecard	Approval of 2015/16 scorecard
3 year Business plan	3 Year Business plan
Business Transformation	Progress update on Business Transformation, cost reduction and run rate for 2015/16
Financial Services	Progress update on FS delivery and strategy for 2015/16

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Annex B: Strategic communications timeline – November 2014 to February 2015

As discussed at the October Board, we discussed the risks the business faces in managing its complex set of stakeholders. It was agreed we would keen the Board updated on key stakeholder events which are captured in the diagram below.



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POST OFFICE LTD EXECUTIVE COMMITTEE

Business Transformation Programme

1. Purpose

The purpose of this paper is to update the Post Office Board on:

1.1 The roadmap and financial flightpath identified as part of Stage III of the Business Transformation design phase;

1.2 The levers we have identified to adjust or accelerate aspects of our strategy in order to respond to the risks and opportunities that emerge as we implement our plans ('Plan B' options);

1.3 Our proposed next steps to effect an orderly transition to the implementation of this roadmap; and

1.4 Progress in the delivery of short term sustainable cost saving.

The Board is requested, after review of this paper, to support the:

1.5 Business Transformation Programme recommendation to progress the transition activities, noting the risks as set out in the paper and reading room deck

The Board is also asked to note the:

1.6 Proposed Transformation programme governance and control framework which will be operationalised during the transition phase

1.7 Programme proposal to update the Board in Q4 2014/15 to confirm the transformation programme plans and outcomes for 2015/16 and beyond, which will be summarised alongside the three year plan and 2015/16 budget updates.

1.8 Business Transformation Programme design conclusions, as a key enabler to the execution of the agreed business strategy and commitment to commercialise the business

2 Context

2.1 The November 2013 Strategic Plan set POL on the road to deliver a commercially sustainable business by 2020 framed by our declared purpose and customer promise. Since establishing this intent we have:

- Concluded the design phase of the business transformation programme and set out the next steps to take an integrated portfolio of business wide change forward. *It should be noted that the current FTE and cost numbers at this stage are directional and indicative – more detailed operational and financial plans will be developed as part of the implemtation phase we are now commencing, as described below;*
- Started to develop an integrated narrative to engage our customers, staff and agents in the process of the change we are going through to deliver our vision of a modern, commercially sustainable Post Office;

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- Defined in more detail our core commercial strategies to defend our position in the mails market by becoming the most convenient parcels retailer in the UK; and establishing the Post Office as the leading challenger in financial services;
- Set out our People and Engagement strategy and action plan to support the transformation of the business in line with the requirements of the POL transformation programme and commercial strategies
- Developed a robust set of options to adjust our strategy to respond to the numerous risks and challenges facing the business.
- Accelerated our business wide near term cost out planning and execution
- Delivered significant progress to date in three out of the six programme themes this paper addresses: Network (NT & Crown), IT (separation), FS (sales).

3 Business Transformation - Design Phase Summary

3.1 The Business Transformation design phase, which mobilised in June 2014, targeted the identification of measures to deliver a £200m - £250m[1] pa improvement in EBITDAS performance by 2019/20 (measured against a 'do nothing' counterfactual which forecasts a £141m EBITDAS loss in 2019/20 arising from income remaining flat and non-agents pay costs increasing in line with inflation). Achieving this level of performance improvement would enable us to reach our objective of commercial sustainability by 2020 in spite of the significant trading challenges we face.

3.2 The programme was divided into three stages:

- A "Current State" assessment; which concluded at the end of July. It identified potential near to medium term cost improvement of circa £100m which was risk adjusted down to £89m at the end of Stage II.
- A high level "Target Operating Model" design stage; which concluded mid-September outlining the measures that would be required to secure a further potential £100-150m of business improvement.
- The Transformation 'Roadmap' stage, which concluded at the end of October with the delivery of a high level implementation plan, financial projection, risk assessment and mitigation plan.

4 Key Findings from Stage III

4.1 The majority of the key findings from Stage II have been preserved in the roadmap and financial glidepath set out at the end of Stage III.

4.2 A summary of the key findings at the end of Stage II are set out below to recap on what was discused in September:

- Restructure of the Crown and Agency network enhanced by a significant extension in the number of outlets, in line with our 'Win in mails' strategy - ***albeit the original plan has been refined significantly in order to maximize value for money and live within the funding envelope we have available through to 2017/18. Key changes have involved retaining a higher number of Crowns, mains and community branches than in our ideal case.***

[1] The £300m figure shown at the end of stage II included £70m of EBITDA improvement from contractualising our social provision. This amount has been excluded from the analysis at this stage to enable a like-for-like comparison of our underlying financial performance, although as noted below we will be conducting further work to update the definition and funding arrangements for our social provision.

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- Execution of the Financial Services Strategy (via Titan / Hawk etc.) in line with the plan outlined to the Board.
- Re-basing agent fee structures resulting from the radical simplification and digitalisation of our products and customer experience.
- Restructure of supply chain and branch support activities. As described at the end of Stage II the current design stops short of outsourcing of supply chain and is instead focused on optimising the existing operation. ***Note: as part of the work on levers to adjust our strategy we are exploring the potential to reconfigure some of our existing product set in order to better control cash demands on the network in a way which might make it viable for a greater proportion of branches to be self-funded (from their own retailer cash), and potentially enabling an outsource solution within the plan period.***
- Retention of a smaller corporate centre to drive strategy and policy, which owns the POL Brand and licences it to our market facing businesses (e.g. POMS) This may be extended to cover a number of commercial portfolio diversification options which will be developed over the plan period
- Transformation of POL technology and digitalisation of the business (cloud solutions, towers procurement and build out of Common Digital Platform) enabling the migration from legacy systems to drive a step change reduction in operating costs and by putting digital at the forefront of all we do.
- Where the business case shows additional benefits, the transfer of operational support activity into a business process outsourcing utility, if necessary, following the 'leaning' of their current activity.

4.3 The Board also received an update in October on the People and Engagement Strategy and how this work is aligned with and supportive of the Business Transformation, in particular;

- The need for higher levels of engagement with and from our employees and agents.
- Reshaping the organisation and the identification of new skills and capabilities required to attract, develop and retain key staff to execute the transformation.
- Develop a commercially focused approach to our customer and agent relationships to drive a more agile and cost effective way of working.

4.4 The main challenge in Stage III was to design a roadmap and financial glidepath that is capable of supporting the delivery of POL's EBITDAS target to 2019/20, and in so doing:

- Deliver over time, a sustainably lower and increasingly variable cost base with an acceptable risk profile.

4.5 A set of design principles, based on the accelerators that were communicated to the business, have been agreed that provide the framework for the Transformation:

- We will disaggregate major change programmes from business as usual activity
- We will prioritise resources and stop programmes that distract, optimising our commercial portfolio across all four pillars and our channels mix.
- We will appoint a single point of accountability for each programme, supported by dedicated delivery resources, quantitative KPIs and an overall delivery plan with key milestones to track progress against;
- We will accelerate significant and complex programmes which are crucial to drive benefit in and of themselves, or which enable the delivery of other business benefits and key TOM attributes

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- We will invest in a number of crucial 'enabling' activities including Transformation Management Office (TMO), Business Case and Benefit Management and Risk & Assurance
- We will limit other change activity, outside of the programmes included in the Transformation portfolio, to ensure we dedicate efforts and resources on major value adding programmes
- We will maintain a focus on the key areas of Communications and Stakeholder Management as we progress through this journey

4.6 The high level Transformation Roadmap comprises the continuation of a number of significant existing in-flight programmes which have previously been discussed in detail with the Board (such as our Mails and FS strategies, People and Engagement and Network Transformation) supplemented by a number of new incremental initiatives which, when taken as a whole, deliver the required business strategy and structural outcomes by 2019/20.

4.7 The transformation roadmap is structured into six themes to balance certainty of outcomes, benefits, cost to deliver and risk. The six themes are owned by ExCo members and are set out below:

- Reduce central costs
- Transform the organisation
- Lean IT; via technology transformation and digitalisation
- Reduce and variablise network costs
- Win in Mails
- Grow Financial Services

4.8 Within the six themes there are 13 discrete programmes as follows;

Themes	Initiatives
Reduce central costs	1a. Near/Mid-term cost out 1b. Finance / HR transformation 1c. Network support transformation 1d. Longer term efficiency - continuous improvement
Transform the organisation	2a. Organisation Design and People Development
Lean IT	3a. IT transformation to significantly lower costs 3b. Digitally enabled business transformation
Reduce and variablise network costs	4a. Network transformation 4b. Crown transformation 2 4c. Customer journey simplification
Win in Mails	5a. Network extension 5b. Commercial portfolio development
Grow Financial Services	6a. Financial Services portfolio delivery

4.9 Each programme within the six themes is summarised in a separate document lodged in the reading room. (Appendix 1).

4.10 The high level Transformation Roadmap will undergo further refinement and development during the transition into implementation, as the outcomes from the individual programme design work is completed and calibrated into the overall delivery plan.

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4.11 At the end of Stage II, we provided a summary of the key risks for the programme. Having concluded Stage III, our view remains that the transformation of POL is a high risk, multi-year undertaking with an uncertain outcome delivered against the backdrop of a very challenging trading environment. In particular, the successful delivery of the transformation is predicated on the following 'need to be true' criteria, all of which entail significant risk:

- The strategy and financial performance in all business areas is delivered in line with current plans and we suffer no material customer attrition resulting from the execution of the transformation plan;
- Government and other institutions (e.g. European Commission) maintain their support for the significant changes proposed;
- POL will manage a significant volume of transformational change while successfully discharging its 'business as usual' agenda;
- Large scale staff change will be driven forward in a complex and at times difficult union environment;
- POL will attract, incentivise and retain top tier talent to drive the business forward in a period of unprecedented change and uncertainty;
- Key partner interests (including BoI, Royal Mail and the NFSP) will be aligned with POL's to drive key changes forward;
- Legacy technology can be overhauled and transformed in a relatively short period of time, leveraging the skills and experience of selected partners.

4.12 The risks are unlikely to materialise in isolation and we need to remain mindful of the compound effect. We have prepared detailed risk assessments in Appendix 2. Given the high level of delivery risk we propose to manage the risk by: prioritising cost out initiatives, which have fewer external dependencies than revenue growth; ensuring strong execution using appropriate partners; avoiding "stranded investment" by developing operational plans and testing external dependencies early; and tracking and assessing delivery centrally and course correcting where needed.

4.13 It should also be remembered that the 'do nothing' option is not without risk – on the contrary, without embarking on this transformational change the Post Office faces the prospect of accelerating market declines and increasing losses, set against the backdrop of a fiscal environment which is likely to limit the ability and willingness of the Government to support the business at historic levels of funding. We therefore believe that there is no credible option but to continue with the transformation of the business that is already under way – and which is already delivering steady improvements in underlying profitability. However, clearly this must be underpinned by a robust and mature approach to managing and mitigating the inevitable risks and challenges we will face over the coming months and years.

4.14 We modelled financial sensitivity of the potential outcomes using the following scenarios:

- our 'central planning range', which is based on the following top and bottom case scenarios:
  - **'full delivery' (the green line in the chart below)** - full delivery of the cost out measures (detailed in the accompanying slide deck) alongside full delivery of the risk adjusted FS growth plans agreed with the Board in September (£508m revenue by 2019/20, equivalent to 8.9% annual average growth) and our plans for defending our position in the mails market (resulting in 1.7% annual average growth in mails income). These are the figures which we will be targeting, while recognising the downside risks;
  - **'partial delivery' (the yellow line in the chart below)** - a 30% reduction in the level of gross savings realised; network extension only serving to defend existing mails income (which is assumed to grow at 0.6% pa overall); and FS growth only reaching £460m by 2019/20 (i.e. all of the risks categorised as

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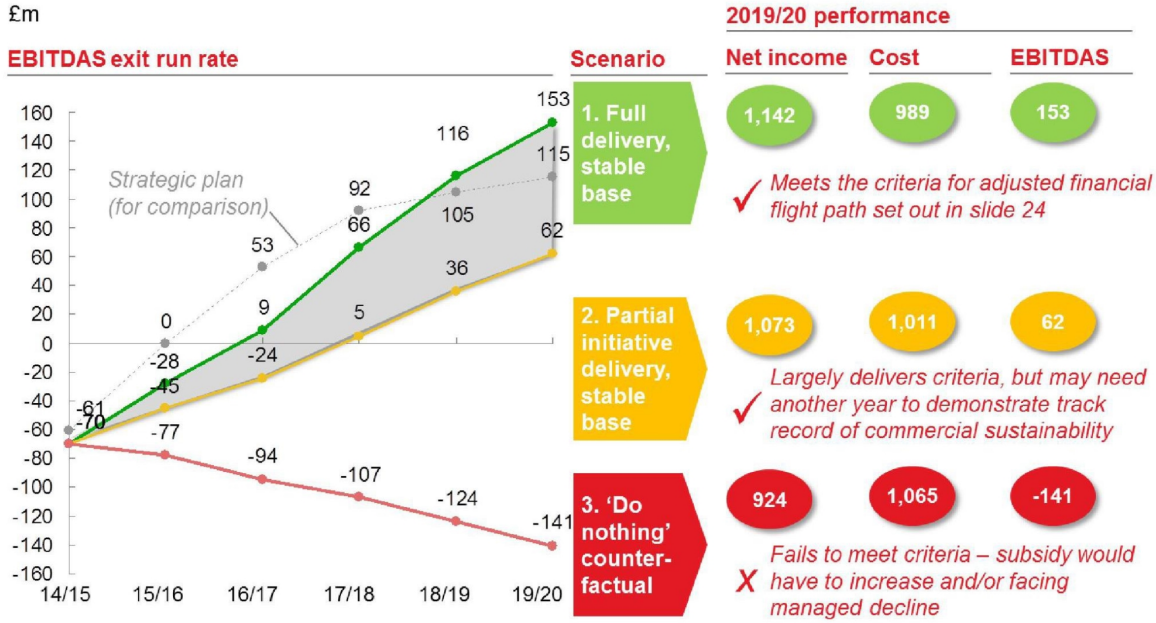
'medium' in the September strategy paper are assumed to materialise, resulting in lower growth of 6.7% pa);

- **the 'do nothing' scenario** explained above (i.e. flat revenue position with non-agents pay costs increasing in line with inflation) – this is the red line in the chart below. (NB we have used these same base case assumptions to model the incremental impact of the Business Transformation initiatives which are included in the two other scenarios noted above).

4.15 These scenarios project a range of EBITDAS outcomes to 2020 which have been compared to the November 2013 Strategic Plan illustrated on the graph below. As this sets out, at the top end of our planning range (which we are targeting) we would deliver breakeven in 2016/17 (one year later than originally envisaged in the Strategic Plan) and a substantial EBITDAS surplus by the end of the decade which exceeds the figure envisaged in the Strategic Plan. At the bottom end of our central planning range, breakeven would be achieved a year later in 2017/18.

4.16 It should be noted that to enable a like-for-like comparison of underlying performance in all of these scenarios we have excluded any benefit from HMG payments for our social provision, although we are nonetheless carrying the net costs (estimated at £70m pa by 2019/20) of maintaining the Community branches. This therefore represents an upside opportunity to our EBITDA performance (i.e. the figure would be uplifted by c£50-70m if we were able to count the associated income from government as a service payment).

4.17 A more detailed assessment of these scenarios and the implications are set out in slides 17-24 of the main deck.



4.18 Underpinning the financial scenarios and roadmap is the expectation of significant cost reduction. Based upon the high level plan we are projecting a 30% reduction in central costs (£54m in 14/15 + £146m by 19/20) and a 16% reduction in agents pay (£74m), on a like for like basis using the 2014/15 as the base for measurement. This equates to an overall cost reduction of 26% and is illustrated in the table below:

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Costs £m	Impact of 14/15 cost-out initiatives	19/20 baseline	Impact of cost out initiatives	19/20 after cost out	Impact of growth initiatives	19/20 after cost out and growth
Central costs	54	602	-146	456	129	585
Agents pay	-	464	-74	390	15	405

4.19 Consistent with the significant reduction in costs the programme is projecting a reduction in FTEs over the plan period. The projected 'end-state' FTEs is greater than originally envisaged (circa 600-800 FTEs) primarily due to the in-house operation of the supply chain business and the retention of a majority of the Crown branches.

4.20 The overall funding required to deliver our original preferred business outcomes (as set out at Stage II) totalled around £1.6bn, exceeding the funding envelope we have available. We have therefore recalibrated the roadmap and financial glidepath, in particularly reducing the numbers of Crown branches that are exited and identifying savings in the projected NT expenditure, in order to bring the funding required within the available envelope. The table below sets out this updated assessment:

	2015 / 16	2016 / 17	2017 / 18	2018 / 19	2019 / 20
Available funding:					
Government funding	280	220	140	60*	50*
Total cumulative funding envelope (incl cash reserves)[1]	**929**	**1,052**	**1,188**	**1,281**	**1,394**
Required funding					
Total cumulative programme funding	380	706	858	904	945
Other essential capex (cumulative)[2]	30	60	100	150	200
Total cumulative funding needs	**410**	**766**	**958**	**1,054**	**1,145**
Headroom against funding envelope	**519**	**286**	**230**	**227**	**249**

1 – Balance sheet modeling assumes the bottom end of our EBITDAS planning range as set out on slide 26. *Also assumes £60m/£50m of HMG funding in 2018/19 and 2019/20, as per 2013 Strategic Plan assumptions. 2 – Provision for other essential capex and change costs (estimated).

4.21 It should be noted that our capital position nonetheless remains heavily constrained over the plan period, with limited scope to absorb new risks or priorities. Discretionary spending will therefore have to be very tightly controlled throughout the period, with strict disciplines in place to ensure that resources are only released once it has been reconfirmed that: a) the initiative remains a priority within the context of our overall strategy; and b) it is affordable within the context of our latest trading and balance sheet position.

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5 Levers for adjusting our strategy

5.1 Given the potential for significant variation in the business and associated financial outcomes over the plan period, we have defined three broad strategic levers that will be used to adjust and recalibrate our plans to respond to new risks, challenges and opportunities as they arise. The levers are integrated into the overall transformation plan and are summarised below and set out in more detail in the accompanying slide deck:

- **working with other key business partners** – in particular given the critical dependencies on Royal Mail and the potential limitations in their ability and/or willingness to fully align with our strategic goals, it is appropriate for us to consider the spectrum of options available to reduce this dependency. Inevitably there are significant financial, legal and operational risks associated with some alternative options, but they should be considered seriously given the existential risks we would face in the longer term if it proves impossible to achieve the level of alignment and performance required with RM;
- **adjusting the channel mix and pursuing further cost savings** – the proposed target operating model already entails a substantial shift to lower cost and more profitable branch operating models and greater use of digital and direct channels in certain product areas such as insurance. Therefore the opportunities to go beyond these existing plans within the next three years are incremental rather than radical (particularly given that our strategies in both mails and FS have defined our branch network as our fundamental USP). However, there are a number of options which we are actively reviewing:
  - **in all scenarios we will dynamically manage the shape and size of our branch network and face-to-face capabilities in order to respond to evolving market conditions** – for example there will be checkpoints throughout the programme to test whether the business case still exists for layering in additional costs associated with new access points and Financial Service Specialists;
  - **we are exploring the opportunities to accelerate and enhance the way we use direct channels to generate new sales growth** – for example depending on market conditions there may be a case for shifting some of our incremental investment away from the branch network towards new or existing products which are primarily sold online (insurance, home services, IDA and associated digital services for public and private sector service providers); we are also reviewing the scope to monetise our data assets and sell advertising access to our digital media to other businesses. The potential financial impact of these measures will be assessed as part of the next stage of work to develop these ideas in more detail;
  - **we will also explore the scope for going further in reducing our cost base**, in particular in supply chain (as noted above) and in agents pay for example through product rationalisation (stripping out low margin products), accelerating work to change the tax status of agents and in the longer-term further realignment of pay rates in light of evolving market benchmarks (which are likely to continue falling).
- **Strategic portfolio management** – while we have now clearly defined our two core pillars of FS and mails, there remain a number of commercial options we can consider to reallocate resources both within these areas and across our other two pillars of government services and home services. This needs to be an active and on-going process to ensure our scarce capital is allocated to the areas of highest profitability and return on investment. In particular, we are:

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- **reviewing the strategic options within Home Phone and Broadband** (where there are credible options either to pursue EBITDAS accretive growth or to divest of the business either through a conventional sale or license arrangement, which could potentially release £40-70m of capital);
- **monitoring the potential to acquire full ownership of FRES** (depending on how the current negotiations with BoI proceed) – this would deliver a significant step-up in EBITDAS of IRRELEVANT pa, but the significant upfront cost (estimated at IRRELEVANT is unlikely to be affordable unless it can be externally financed;
- **exploring the opportunities to leverage our brand equity and customer reach** (both in-branch and online, particularly if we move into IDA) to exploit new areas of growth that may become increasingly important if we face declines in our traditional products. The income from such initiatives is likely to be modest, but if they can be deployed at low margin cost (for example through license arrangements with a third party) they have the potential to be EBITDAS accretive;
- **exploring the options to strengthen our proposition to host retailers**, recognising that we need to defend or grow these relationships in order to fulfil our ambitions in the mails market, and;
- **updating the definition and funding arrangements that underpin POL's 'social provision'.** This comprises the delivery of commercially unviable services that drive accessibility for remote regions and disadvantaged groups. Further work will be undertaken between now and spring 2015 to define the precise options for what is ultimately considered for inclusion within 'social provision' and to ensure that this part of the business is treated as an integral part of the network going forward. This work will include exploring the potential to move to a contractual service payment to underpin this work rather than the current subsidy arrangements, although it should be noted that there are pros and cons with both options.

5.2 None of these levers provide a silver bullet to fully mitigate the risks we face. Therefore given that income risk is skewed to the downside our top priority will be on accelerating the reduction and variablisation of our cost base to ensure the business has the flexibility and resilience to respond to a range of market conditions.

6 Transition to Business Transformation implementation

6.1 The transformation will require a 'top down' integrated governance and control structure to ensure value is delivered in line with the plan. The proposed governance model consists of a Chief Transformation Officer, supported by an enhanced Transformation Management Office. All Transformation programme plans and commercial business cases will be scrutinised by the Finance Committee and a new Enterprise Design Authority with ultimate approval sanctioned and controlled by the Transformation Committee.

6.2 Each programme will be sponsored by an ExCo member who will be accountable for the approved business outcomes, the associated benefits, cost to deliver and risk management.

6.3 A summary of the governance and control framework is provided in the supporting material lodged with the Board in the reading room.

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6.4 There are a number of key activities required to be completed to set up the transformation implementation for success and manage the substantial risks which have been identified. They are summarised below:

- Progress all 'in-flight' programmes that are consistent with the high level roadmap, with regular updates provided to ExCo and a revised Transformation Portfolio governance forum;
- Further development of our integrated narrative to engage customers, staff and agents in the change journey;
- Appointment of Programme Directors / Leads to ensure the overall transformation portfolio of initiatives are progressed uniformly from 2015/16 onwards;
- Simplify the ExCo and SLP organisation with clearer roles and responsibilities by completing the planned organisational re-design;
- Accelerate the development of the Transformation Management Office (TMO) and the Risk & Compliance function so as to provide leadership support to the ExCo, as recommended by the recent PwC report / McKinsey;
- Develop programme delivery and resourcing plans during H2 2014/15 for all initiatives due to be progressed on the roadmap in 2015/16;
- Secure relevant partner support by adjusting existing partner contracts or contracting new partners (as appropriate);
- Incorporate, as appropriate, the recommendations from the recently commissioned Business Transformation assurance review performed by PwC which has been lodged with the Board in the reading room;
- Demonstrate POL's ability to deliver substantial near term cost efficiency by driving out the targeted in-year improvements in H2 2014/15

6.5 The actions required to be progressed and concluded during the transition period, which is expected to conclude by the end of 2014/15, will be monitored by the Transformation Committee.

6.6 We propose a further Board update in the New Year, which will coincide with the 3 year operating plan and budget update. The update will seek to confirm that sufficient progress has been made during the transition period to support the recommendation for the transformation implementation to be progressed as an integrated portfolio of change from the start of the new financial year.

7 In year cost savings update

7.1 Stage I of the programme identified annualised cost saving opportunities in the order of £100m (risk adjusted to £89m at the end of Stage II) to be achieved by the end of financial year 2015/16.

7.2 The business is progressing these savings as part of an integrated business wide cost reduction programme, governed by a sub-committee of ExCo. This sub-committee, the Cost Reduction Group (CRG), meets weekly to assess progress and to agree actions as appropriate

7.3 The programme delivery is broken down into phases with an initial priority on delivering £60m of in-year savings in 2014/15 (up from the £46m in the budget)

- £53m is baked into the ExCo functional targets.
- A portfolio of cost efficiency savings have been identified, by ExCo function, to deliver the required improvement
- A number of 'business wide' initiatives have been identified in the event that functional savings fall short of targets. These include significant actions on both

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staff and non-staff costs, a number of which have been recently communicated to colleagues.

7.4 The priority for 2015/16 will be on delivering further savings that, combined with the savings delivered in 2014/15, deliver the original target of £100m of annualised cost reduction.

7.5 Assuming the in-year savings for 2014/15 are delivered this will contribute £54m of recurring savings. This is ahead of the £48m originally set as a target. The remainder (£46m) currently comprise;

- Staff initiatives to be launched at the end of November will contribute a further £15m
- A potential further £6m of Staff initiatives to be launched in the new year that will require more detailed analysis and validation prior to implementation
- A further £10m - £15m of Non-Staff (Supplier) cost reduction initiatives arising from the recent supplier 'town hall' meetings and further focus on those suppliers where we spend over £100k per year.
- The Mid-Term initiatives originally identified in Stage I which have been analysed further and adjusted down to £16m. These include a range of product rationalisation, optimisation and automation opportunities across a range of functional areas and in a number of cases cross functional change to release value

7.6 Delivery of the cost improvement is a business priority and recognised as a crucial first step in the execution of the business transformation. The targets for the required cost reduction will be factored into the three year plan and specifically the 2015/16 budget to underwrite the £100m saving by the end of 2015/16.

8 Request

As set out in section 1 of this paper the Board is requested to support the:

8.1 Business Transformation Programme recommendation to progress the transition activities, noting the risks as set out in the paper and reading room deck;

The Board are also requested to note:

8.2 Business Transformation Programme design conclusions, as a key enabler to the execution of the agreed business strategy and commitment to commercialise the business;

8.3 Proposed Transformation programme governance and control framework which will be operationalised during the transition phase; and

8.4 Programme proposal to update the Board in Q4 2014/15 to confirm the transformation programme plans and outcomes for 2015/16 and beyond, which will be summarised alongside the three year plan and 2015/16 budget updates.

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Work in progress draft

Becoming a commercially sustainable Post Office

Business Transformation Programme – Stage 3

Board update
25th November 2014

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Executive summary

- **The November 2013 Strategic Plan set a path to deliver a commercially sustainable business by 2020.** We have defined our strategies to defend our position in mails and establish the Post Office as a leading challenger in Financial Services. However, achieving commercial sustainability also requires a new operating model that right sizes our cost base to enable us to survive in a challenging market environment with a growing number of low cost competitors, whilst remaining true to our purpose and brand promise throughout the transformation.
- **We have defined a new target operating model,** with a streamlined corporate centre, franchise network and bulk outsourcing of transaction support, resulting in a significantly lower cost base and FTE profile (~30% reduction in central costs[1], moving from 6,132 to 4,105 employees).
- **Given Post Office's assessment of its starting point, the transformation needs to be driven from the top-down, focusing on a small number of significant change initiatives.** The proposed roadmap is structured into six themes to balance outcomes, benefits, certainty of outcome and risk – (1) reduce central costs; (2) transform the organisation; (3) lean IT; (4) reduce and variabilise network costs; (5) Win in Mails; (6) Grow Financial Services. Within the six themes, there are 13 discrete programmes.
- **There are significant risks in transforming and sustaining the target business model**, including major programme delivery risks, alongside a number of reputational and operational risks that could impact our customers. These risks are unlikely to materialise in isolation, and so we also need to be very mindful of the compound impacts.
- **We have tested the financial impact of the overall transformation using various scenarios.** At the top end of our central planning range we achieve breakeven in 2016/17 and an EBITDAS in 2019/20 of £153m. At the bottom end of our central planning range, we achieve breakeven in 2017/18. The plan is to drive for the top end, however we have a set of leading indicators to dynamically manage the plan if we come under pressure. We have adjusted the programme funding requirements to keep within our existing envelope - but with headroom falling within £200m by 2017/18 our scope to absorb new risks/priorities is limited
- **We have outline three broad levers to adjust our strategy to respond to the key risks and challenges**, including (1) working with other partners; (2) adjusting the channel mix; (3) portfolio management. None of these levers provide a 'silver bullet' to fully mitigate our risks. Given our income risks are heavily tilted to the downside, our top priority will be on variabilising and reducing our cost base as quickly as possible to ensure the business has the flexibility and resilience to respond to a range of market scenarios.
- **The transformation requires "top down" integrated governance and control to ensure the value is delivered in line with plan.** The proposed governance model consists of a Chief Transformation Officer, supported by an invasive TMO, Enterprise Design Authority and Transformation Committee. We also need to ensure that we have a compelling story throughout our journey so we attract and retain colleagues and customers.
- **The next few months will focus on putting in place the critical success factors ahead of intermediate checkpoint reviews before implementation,** covering: (1) setting up the TMO; (2) recruiting delivery partners; (3) fleshing out the IT roadmap; (4) operationalising programmes; (5) building MI capability; (6) delivering the 14/15 plan – in-flight programmes, Wave 1 organisation redesign, and in-year cost efficiencies

1 – does not include cost uplift from revenue growth initiatives

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- **Strategic context and target operating model**
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We have a clearly defined business model that articulates our long-term source of competitive advantage

- The work for the June awayday and September FS deep dive has established clarity around **two core customer propositions with a symbiotic, value-enhancing relationship:**
  - ✓ our ability to challenge in FS is built on the trust and customer reach which goes with being the UK's number one mails retailer;
  - ✓ in turn, our FS product set diversifies our income base and strengthens our offer to host retailers versus the competition.

IRRELEVANT

The most convenient mails & parcels retailer

The UK's leading challenger in financial services

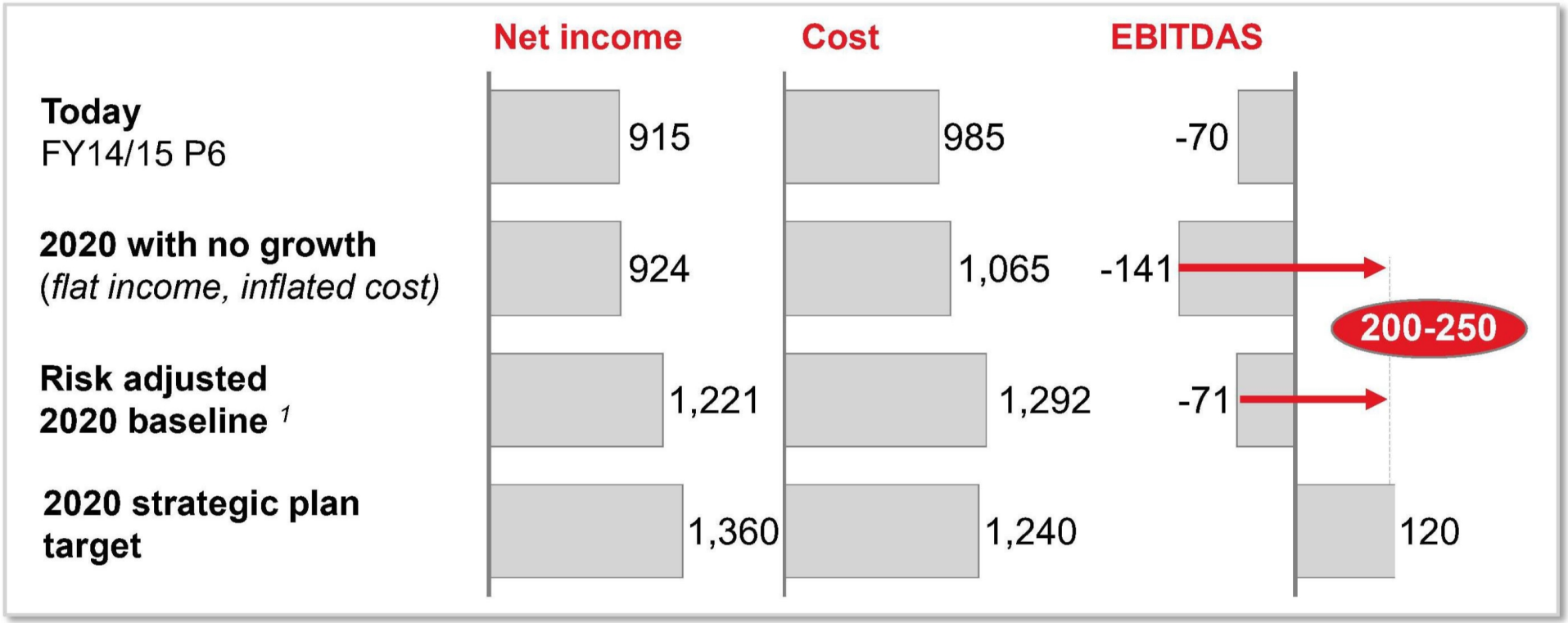


- The Business Transformation programme has defined the operating model (and roadmap) required to underpin these customer propositions, with the following key attributes:
  - **~30% reduction in central costs by 19/20 and variabilisation of network costs**[1] – giving us greater financial and operational flexibility to respond to challenging and uncertain market conditions, while continuing to underpin our customer propositions
  - Accelerating towards our aspiration for a fully franchised network of 20-30,000 outlets. This reaffirms the fact that, **first and foremost, we are a B2B business** – while direct sales can broaden our income base (especially in FS), it is our relationships with host retailers that are the prime source of our long-term competitive advantage, and also the root of our social value (anchoring a retail presence and access to services in communities across the UK)
- The People and Engagement strategy has defined the change agenda for the next 18 months to enable our staff and key stakeholders to support us on the journey to achieve commercial sustainability

1 – Includes £54m cost reduction in 14/15 and £146m incremental cost reduction by 19/20, does not include cost increase due to inflation and revenue growth initiatives

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Commercial sustainability requires a radically different operating model to drive significant performance improvement



£200-250m of cost-out may be required to close the potential for an EBITDAS gap between the 2020 strategic plan target of £120m and the downside projection of -£71m at the June board, leaving contingency in case commercial plan does not fully deliver

1 – June Board strategy figures (incl. Mails income at risk and Network Extension) adjusted for incremental FS income at risk, and exclusion of £130m cost-out built into the June Board plans

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The radically simplified target operating model delivers a lower, variable cost base and 33% fewer FTEs versus today

Automate / lean Outsource / offshore

	Target operating model	Ingoing hypotheses for target operating model design
Business management Responsible for delivery of agreed 3 year operating plan	Customer, Product, Businesses Network management	▪ Radically simplified customer journeys, shifting to online ▪ Leaned business management and clear P&L accountability ▪ Shared Centres of Excellence for customer analytics, account management and marketing across all business lines ▪ Transition to a lower cost agent network, closure of unprofitable Crowns, revised agent pay structure, automated network support ▪ Integrated account mgmt and retail capability (single ownership)
Corporate centre Strategy and policy function setting direction for the organisation	Comms; Finance; People & devm't; Brand; Strategy; Risk and assurance Technology Transformation management office	▪ Talent development programme to attract, retain and incentivise ▪ Licencing of the POL Brand to market facing business/portfolio opportunities ▪ Top-down strategy setting with an integrated roadmap to 2020 ▪ Enhanced risk and change management capability ▪ TMO configured to execute the transformation
Operations Support to business management and corporate centre - bulk processes and service capability	Supply chain Contact centres Partner operations Finance operations HR operations IT delivery	▪ Cash supply chain transitioned to retailer cash where possible. In the short-term, reduced demand for stock supply chain via product simplification / digital migration (no stock supply warehouse) ▪ All business transactional support functions moved to cloud BPaaS offerings where available or outsourced ▪ Reduced business demand on support functions to focus on high value services only

1 – Increase by 2,500 FTE versus indicative numbers at September Board. The main sources of increase are: 1) partial closure of Crowns only (bottom 40%) and 2) transformation of Supply Chain stopping short of outsource
Note: Does not include any FTE increase from revenue plans

Total in-house FTEs: ~4,105 (vs. 6,132 today)[1]
Total costs: ~£1Bn (vs. £1.3Bn projection for 2020)
EBITDAS: ~£153m (vs ~£-141m projection for 2020)

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Target operating model has significantly different attributes to todays ways of working

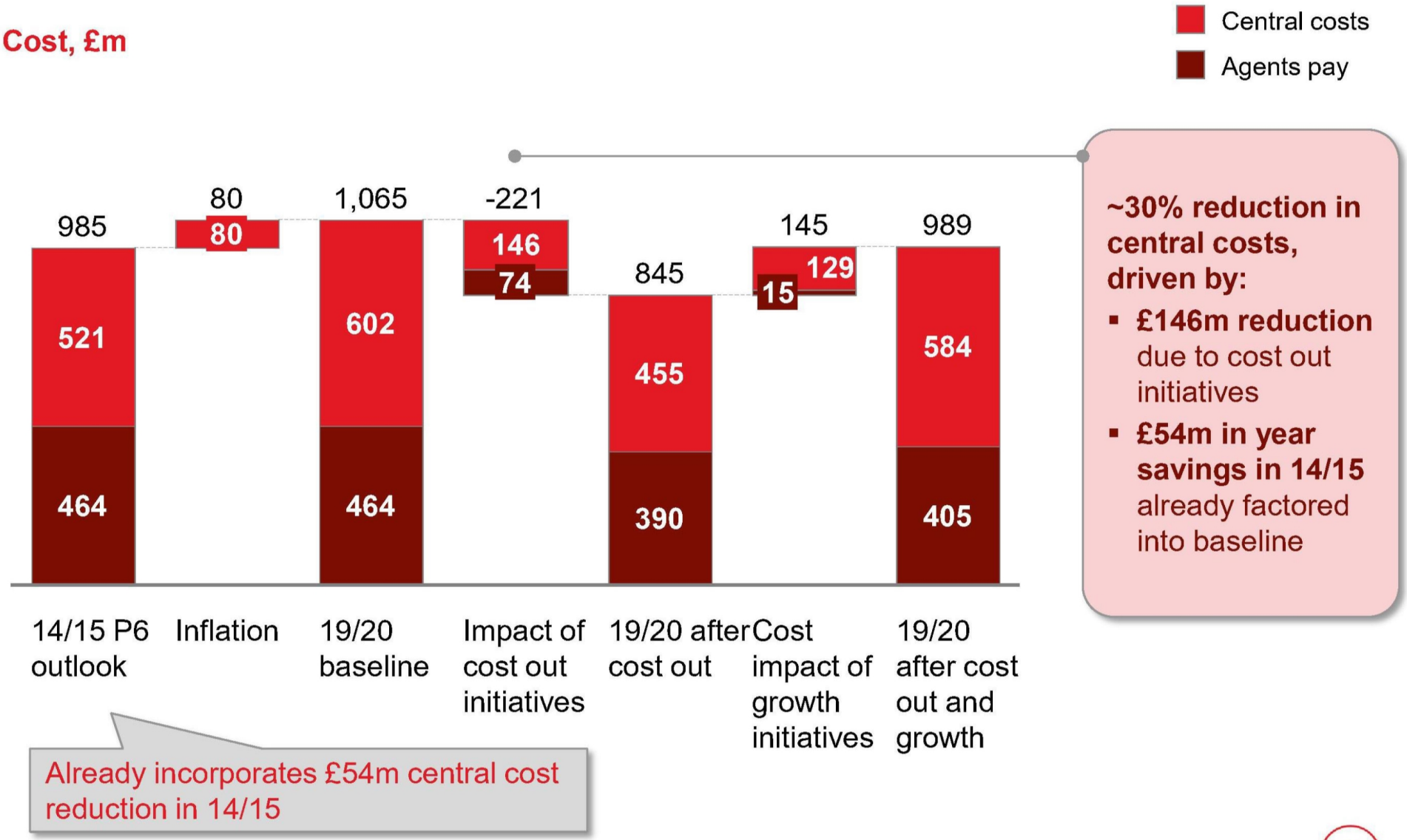
	From	To
Organisation and people	• 6,132 FTE across organization in 2014/15 • Lack of team structure, role definitions and clear reporting lines with an inward, incumbent mindset	• 33% reduction in headcount to 4,105 FTE from cost-out initiatives[1] • New top team OD structure with cascade of communications, strong central transformation governance (CTO, TC) and motivated, accountable colleagues
Processes	• Little use of automation (e.g., workflow, case management, self-service) • Inefficient manual, duplicated and uncoordinated processes • Little process MI (e.g., error rates)	• Processes automated (e.g., self-service) or semi-automated (e.g., workflow) where possible • Streamlined processes with minimal waste, • Continuous measurement and improvement
Data and technology	• Fragmented legacy IT systems that struggle to meet digital business needs and drive inconsistent reporting and manually intense reconciliations	• Lower cost IT landscape that enables Digital Mails and FS growth, and effective MI reporting across POL • Off the shelf vanilla, industry standard solutions where possible (e.g., Finance, HR)
Sourcing	• Transactional support functions heavily insourced (incl. Finance service centre, HR service centre, Network support)	• Transactional support functions centralised in low cost onshore location and outsourced as utility

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1 – FTE increase of revenue growth initiatives to be worked

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We plan to achieve a ~30% reduction in central costs by 2019/20



~30% reduction in central costs, driven by:

- **£146m reduction** due to cost out initiatives
- **£54m in year savings in 14/15** already factored into baseline

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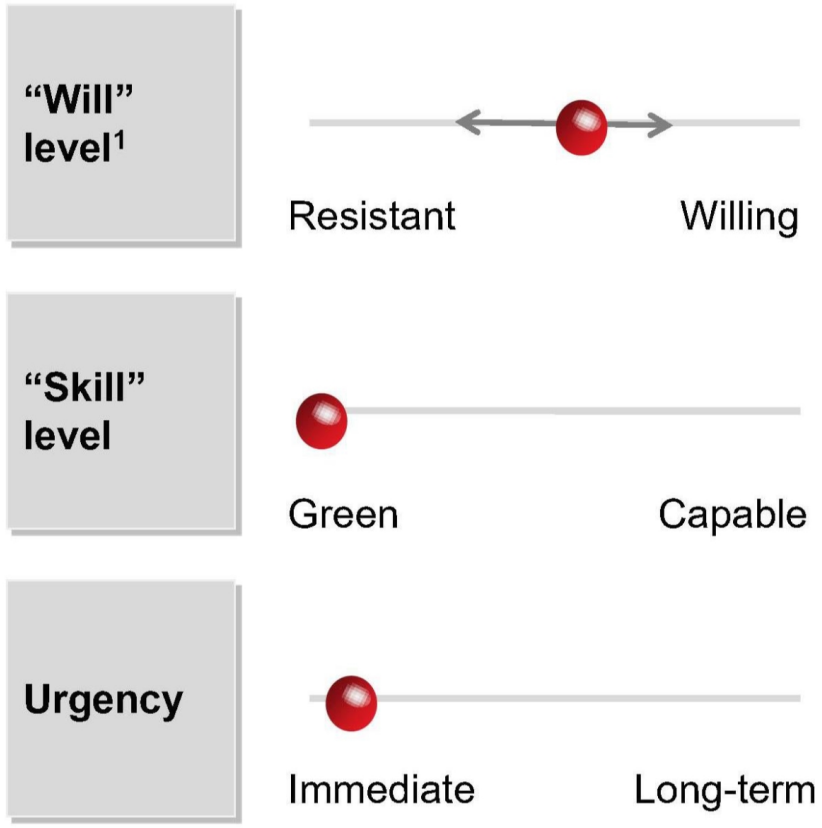
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The roadmap will be driven top down, focused on a small number of change initiatives

Assessment – *based on ExCo input*



Implications for transformation approach

- Leadership directed and outsider supported;
- Single programmatic focus to get the organisation moving in one direction;
- Aligned on a simple set of themes in support of a recognised need to change;
- Prioritised initiatives, boldly stopping initiatives that distract attention and resources;

Implications on POL: For the transformation delivery to be effective, we will require:

- A more top down, directive leadership style;
- A real focus on delivering a limited number of substantive change initiatives, and;
- A business-wide commitment to successfully transform POL at pace.

1 – The only variation in survey results relates to the 'will' level of the organisation. The status of this dimension will be kept under review during the transition to implementation.

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A number of principles have framed the shape and sequencing of the roadmap

- **Disaggregate major change programmes from business as usual activity** with separate dedicated governance forums and supporting MI / control frameworks
- **Plot all major change on one roadmap** to ensure an integrated view for prioritisation of scarce management bandwidth, change capacity, funding and dynamic management of delivery schedule
- **Create a top-down roadmap first and then translate into operational plans**
- **Accelerate cost out programmes that deliver significant benefits,** which are largely within our control and are not dependent on external market factors or business partner engagement (e.g., Royal Mail, Bank of Ireland)
- **House all other change activity within a constrained "small change programme" budget** managed from within the overall Transformation Portfolio to retain control on overall funding/spend and avoid destabilising core transformation programme plans
- **Appoint a single accountable executive (ExCo / SLT) and specific quantitative targets for each programme**, supported by dedicated delivery resources and an overall delivery plan with key milestones to track progress against
- **Put in place the critical success factors before we begin** including TMO, Communications, Stakeholder Management, Business Case and Benefit Management, Risk and Assurance, Governance, Structures Control Framework and supporting MI

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The proposed roadmap is structured into six themes to balance outcomes, benefits, certainty of outcome and risk

£m, FY19/20 impact Theme	Objective	Net income impact	Cost impact	EBITDAS impact	Total funding
Reduce central costs	• Reduce central costs by £79m by driving out near term opportunities, automating/ outsourcing, simplifying the organisation and renegotiating supplier contracts	0	79	79	113
Transform the organisation	• Redesign organisation, refresh performance management, recruit top talent, build capabilities	0	0	0	3
Lean IT	• Move to lower cost towers procurement model, migrate from Horizon and deliver "IT enablers"	0	22	22	185
Reduce and variabilise network costs	• Migrate 88 Crowns to lower, variable cost Agencies • Simplify customer journeys to reduce agent pay • Transition to new agent contracts[2] • Introduce new Locals Lights format	-38	120	82	528
Win in mails	• Become most convenient Mails retails incl. opening 12.5k Access Points, SME proposition, CRM and e-commerce development[1]	79	-64	15	50
Grow FS	• Become the challenger FS provider	177	-80	97	36
Critical enablers	• Establish and operate transformation enablers incl. TMO / Comms / Portfolio Management / Funding	N/A	N/A	N/A	30
Additional funding	• Provision for other essential capex and change costs ("small change budget")	N/A	N/A	N/A	200
Total		218	77	295	1,145

1 Some e-commerce development is enabled by "Simplify Customer Journeys" programme
2 By variablising cost that is currently fixed, this initiative also provides future flexibility in addition to financial performance

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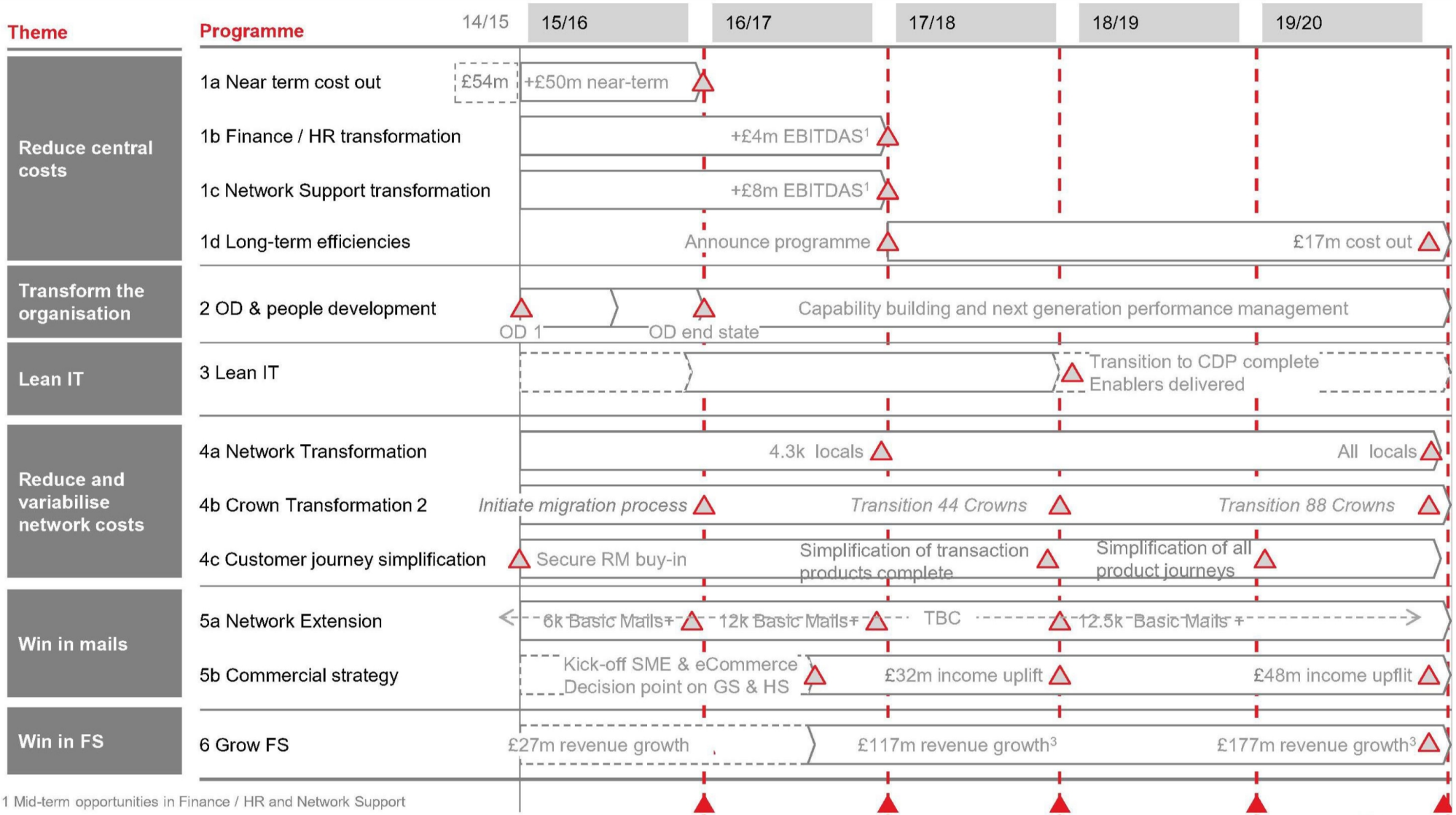
Within the six themes there are 13 delivery programmes*

Theme	Programme		Objective
Reduce central costs	1a: Near-term cost out		• Capture near-term savings to be delivered by March 2016 by leaning/centralising/stopping activity and renegotiating supplier contracts
	1b: Finance/HR transformation		• Capture mid-term savings by March 2017 by automating / outsourcing
	1c: Network Support transformation		• Capture mid-term savings by March 2017 by automating / outsourcing
	1d: Long-term efficiencies		• Drive year on year savings (continuous improvement) in our operations to achieve target end state for the corporate centre
Transform the organisation	2: OD & people development		• Review and refresh organisation design, recruit top talent, refresh performance management system, build capabilities and foster culture change
Lean IT	3: Lean IT	3.1: Lower costs	• Move to lower cost towers procurement model to drive cost efficiency
		3.2: Enable change	• Migrate away from Horizon and deliver "Digital enablers" to support overall transformation
Reduce and variabilise network costs	4a: Network Transformation		• Transform 2,500+ branches to local model, complete transformation of remaining mains and develop and introduce local light'
	4b: Crown Transformation 2		• Current base case envisions migration of 88 Crowns (40% that are deemed unprofitable) to lower, variable cost agencies (primarily Mains)
	4c: Customer journey simplification		• Simplify journeys to reduce agent time, agent remuneration and improve convenience (partially enabled by Network Development)
Win in mails	5a: Network Extension		• Maintain our Mails market share by opening up to 12.5k Access Points over 3 years with targeted multiple retailers
	5b: Commercial strategy		• Become most convenient Mails retails incl. SME proposition, significant ecommerce development, and strategic portfolio management
Grow FS	6: Grow FS		• Become the challenger FS provider in execution of agreed strategy

* Excludes 'enabling' activities for People, Change Management, Communications and Stakeholder Management

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The high level roadmap delivers the target state TOM by 2020



1 Mid-term opportunities in Finance / HR and Network Support

Note: The 'high level' Transformation Roadmap will undergo further refinement and development during 'transition' into implementation (eg Clarification and Transition States), as the outcomes from individual programme design work is completed

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The portfolio has a range of outcomes and financial impacts

£m, FY19/20 exit run-rate impact

Theme	Programme	Net income impact	Cost impact	EBITDAS impact	Total funding
Reduce central costs	1a: Near-term cost out	0	50	50	25
	1b: Finance/HR transformation	0	4	4	15
	1c: Network Support transformation	0	8	8	28
	1d: Long-term efficiencies	0	17	17	45
Transform the organisation	2: OD & people development	0	0	0	3
Lean IT	3: Lean IT[1]	0	22	22	185
Reduce and variabilise network costs	4a: Network Transformation	0	35	35	445
	4b: Crown Transformation 2	-8	24	16	71
	4c: Customer journey simplification	-30	61	30	12
Win in mails	5a: Network Extension	32	-26	6	31
	5b: Commercial strategy	48	-38	10	19
Grow FS	6: Grow FS	177	-80	97	36
Enablers	Establish transformation enablers incl. TMO	N/A	N/A	N/A	30
Additional funding	Provision for other essential capex and change costs	N/A	N/A	N/A	200
Total		**219**	**77**	**295**	**1,145**

1 – See appendix for further detail

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Each programme has been detailed and aligned with its owner, and is summarised in Appendix 1

Executive summary

Programme objectives
- The objective of the CTP2 program is to drive EBITDAS improvement and transition to a lower, variable cost base, thereby reducing risks associated with any net income shortfall
- The principle activities of the program as migration of volume from 305 Crowns network to nearby Agents (primarily Mains)

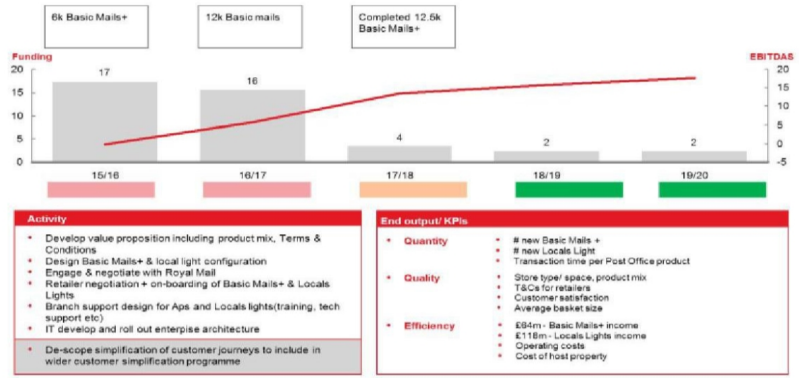
Financial impact
- We assume 81% retention of Crown net income in migration, as consistent with past CTP experience
- We estimate savings of ~£123m in fixed costs)Crowns' staff and property), offset by ~£70m in variable cost increase associated in Agent fees and costs
- We estimate that we will need approximately ~£264m in funding over the course of the migration, driven by staff redundancy (£109m), property repair and dilapidation (£38m), property holdover costs (£65m) and XXX. No delivery partner support is expected.
- This is a conservative estimate; there may be potential upside

Sequencing of initiatives
- In 2015/16, we would prepare for migration of Crown volume through development of a commercial exit and safe passage plan, VR/CR process design and communications strategy and execute a piloting program.
- We would initiate migration process in earnest in FY2016/17 to deliver 50 Crown transitions, ramping up to 75 additional Crowns in 2017/18 and 2018/19, with the full migration completed by 2019/20
- By sequencing Crowns after build-up of Agent network, we have the opportunity to minimize volume lost during the migration

Team structure and delivery partner support
- We estimate that an in-house team of approximately 30 people, combining a mix of finance, network and programme management, to deliver the above-programme
- We expect an element of design partner support will be required to help shape the commercial exit strategy and safe passage plans, with an estimated cost of ~£1m

Risks and mitigation activity
- The largest risks associated involve the CWU (and associated political risk), which have a high risk of undertaking strikes. This risk is expected to peak in Year 2 following communication of the plan, and tail-off thereafter

Fact sheet



Financial plan

£m	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	Total	Assumptions / Drivers
Roadmap: Number of Crowns	305	200	100	0	0	0		
Roadmap: % of Crowns transitioned	0%	34%	67%	100%	100%	100%		
P&L impact: % ramp up of P&L impact	0%	34%	67%	100%	100%	100%		Assumed to be same as portion of Crowns transitions
P&L impact: Income growth								
Total Crowns net income forgone	0	-29	-59	-90	-93	-95		2015 / 16 anticipated net income / Crown of £278k, growth at 3% inflation annually
Net income transitioned to Mains	0	24	48	73	75	77		81% of Crown net income is transitioned to Mains
Crowns net income lost in transition	0	-6	-11	-17	-18	-18		
Cost savings / (spend) impact								
Staff costs								
Plus: Crowns staff cost savings	0	29	57	88	91	93		2015 / 16 anticipated staff cost / Crown of £83m, growth at 3% inflation annually
Less: Mains staff cost outlay	0	0	-1	-1	-1	-1		2019 / 2020 anticipated staff cost / Main of £1m, adjusted for 3% inflation annually
Total staff cost savings / (spend)	0	28	57	87	90	92		
Non-staff costs								
Plus: Crowns property cost savings	0	9	18	28	29	30		2015 / 16 anticipated non-staff cost / Crown of £26m, growth at 3% inflation annually
Less: Mains property cost outlay	0	-2	-5	-7	-7	-7		Mains property costs expected to be 25% of Crown property costs
Less: Mains Agents' Commission	0	-19	-38	-58	-60	-62		Agents' commision blended commission rate of 80% (excludes impact of rebased pay)
Total non-staff cost savings / (spend)	0	-12	-24	-37	-39	-40		
Other costs								
Difference in Corporate overhead	0	0	0	0	0	0		No expected impact to corporate overhead costs
Total cost savings / (spend)	0	16	32	50	51	53		
Total EBITDAS impact	0	11	21	33	34	35		
Funding needs: Staff redundancy costs	0	37	36	36	0	0	109	Redundancy of £38k (~2yr pay) for 2,505 +350BMs employees remaining post-CTP
Property dilapidation costs	0	13	13	13	0	0	38	Expected ~£125k / Crown on average
Property holdover costs	0	23	21	21	0	0	65	50% premium to CTP for remaining 300 Crowns (CTP: £10m on the 70 stores)
Agent set-up costs	0	16	15	15	0	0	46	~150k / Main transferred (CTP experience due to subsidies and other start-up costs)
Other costs	0	2	6	6	2	0	15	Programme team of 50-60 required to oversee programme at £150k average salary
Funding needs	0	90	91	91	2	0	273	

Risk assessment and mitigation plans

	2015/16	2016/17	2017/18	2018/19	2019/20
Summary of risk	• High risk of no agreement with Royal Mail to deliver planned Network • High likelihood of NFSP unrest when announcing and delivering extension • Risk to government appetite and funding	• Risk to implementation from (1) delivering the planned changes to Network in one go (volume of change for business) (2) NFSP unrest likely	• Lower risk to implementation due to lower level of planned change in year; risks from (1) delivering the planned changes to Network in one go (volume of change for business) (2) possible NFSP unrest	• Completed	• Completed
Key overall risks	Royal Mail	NFSP	Government appetite		
Decision points	Agreement with Royal Mail – do not enable significant funding until this is achieved		Agreement with NFSP	Government buy in	Yearly decision point to adjust scope based on market developments
Correlations / dependencies	Significant IT requirements	Dependency on simplified journeys	Correlation with Network Transformation, Simplified customer journeys		

We will align a single senior point of accountability per programme, supported by dedicated delivery resources, quantitative KPIs and an overall delivery plan, incl. key milestones to track against

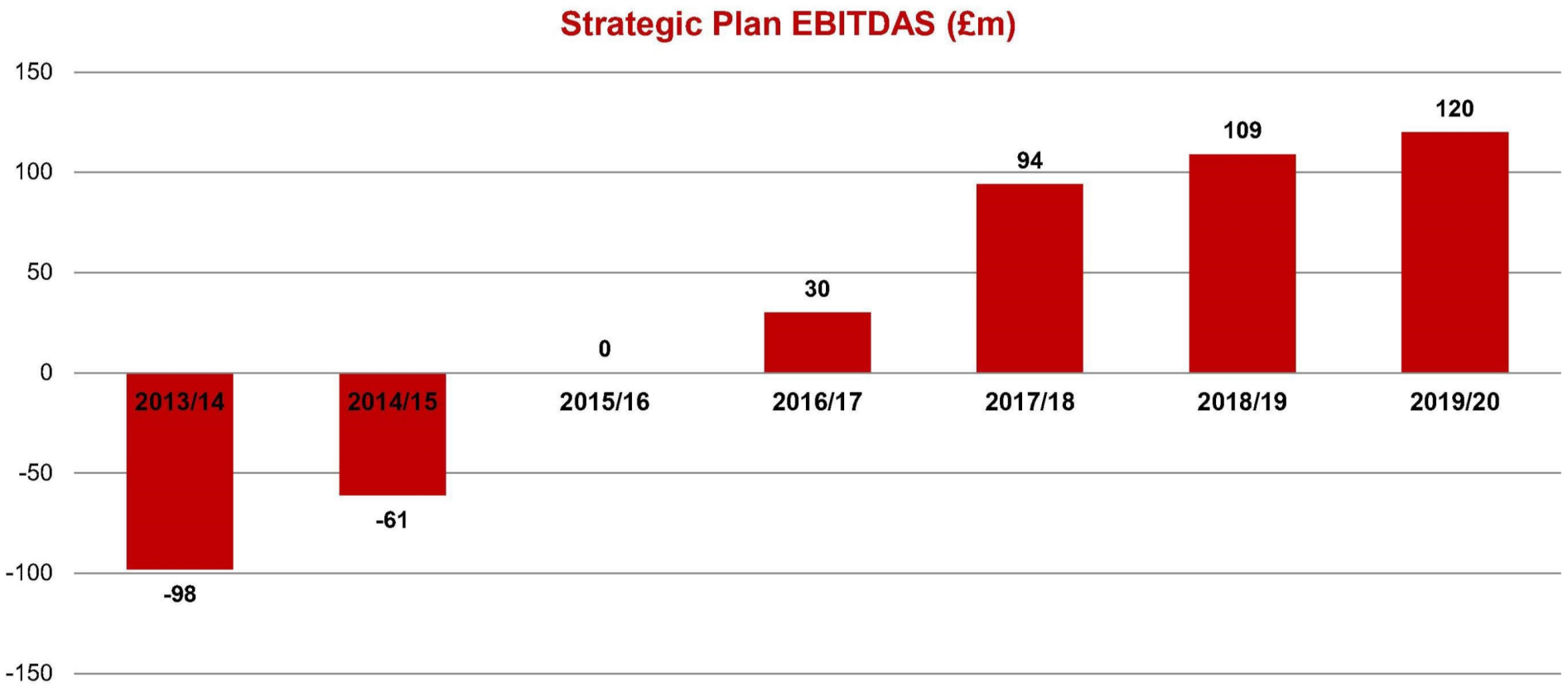
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The financial flight path in the November 2013 Strategic Plan was set with the objective of delivering a commercially sustainable business fit for mutualisation by 2020

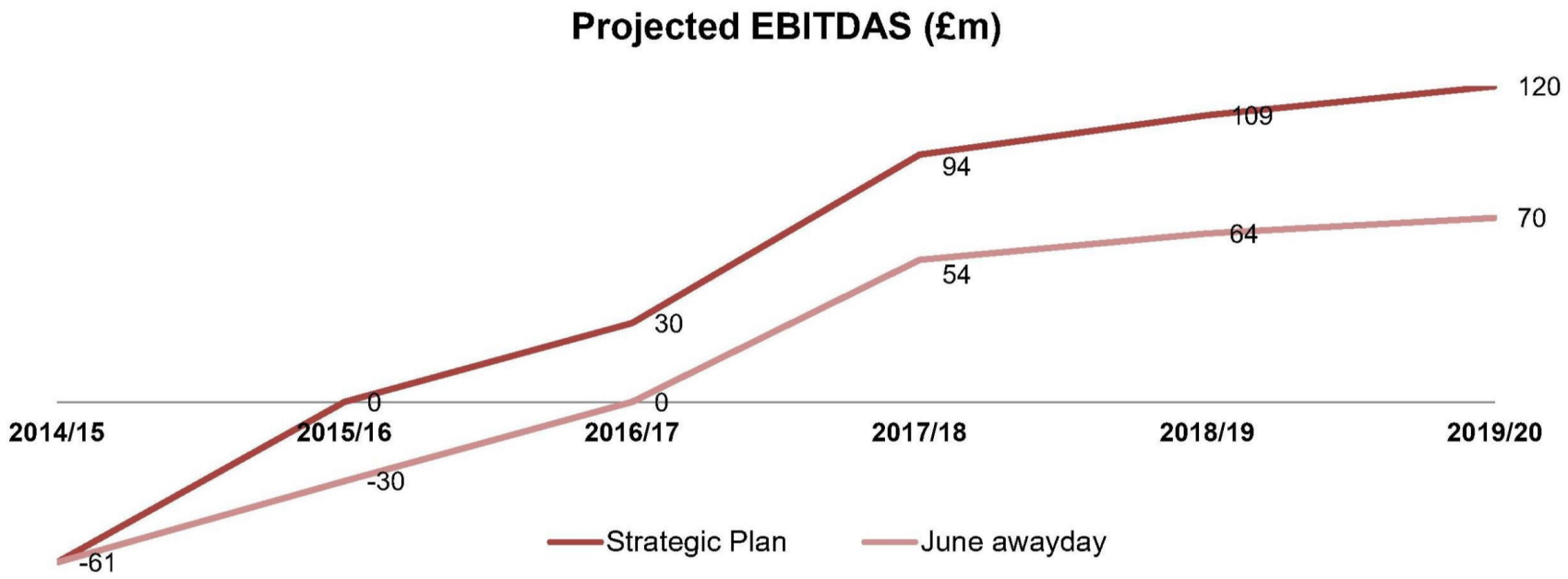


Financial milestones set in Strategic Plan:

- **March 2015** Breakeven in Crowns
- **2015/16** Breakeven EBITDAS
- **2016/17** Positive cash flow
- **2018/19** Track record of commercial sustainability
- **2019/20** Subsidy reduced to £50m pa

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But as we discussed at the June away day, the more challenging market conditions that have emerged over the last 12 months are forcing us to adjust our plans



In addition to the direct impact on profitability, the acceleration in competitive pressures over the past 12 months is forcing us to **take more radical action than we envisaged in the Strategic Plan just to defend lower income numbers** (e.g. network development and product simplification).

This inevitably has capacity implications (e.g. management bandwidth, IT constraints and ability to absorb stakeholder noise) – **making the delivery of our cost savings and overall turnaround more challenging and expensive**.

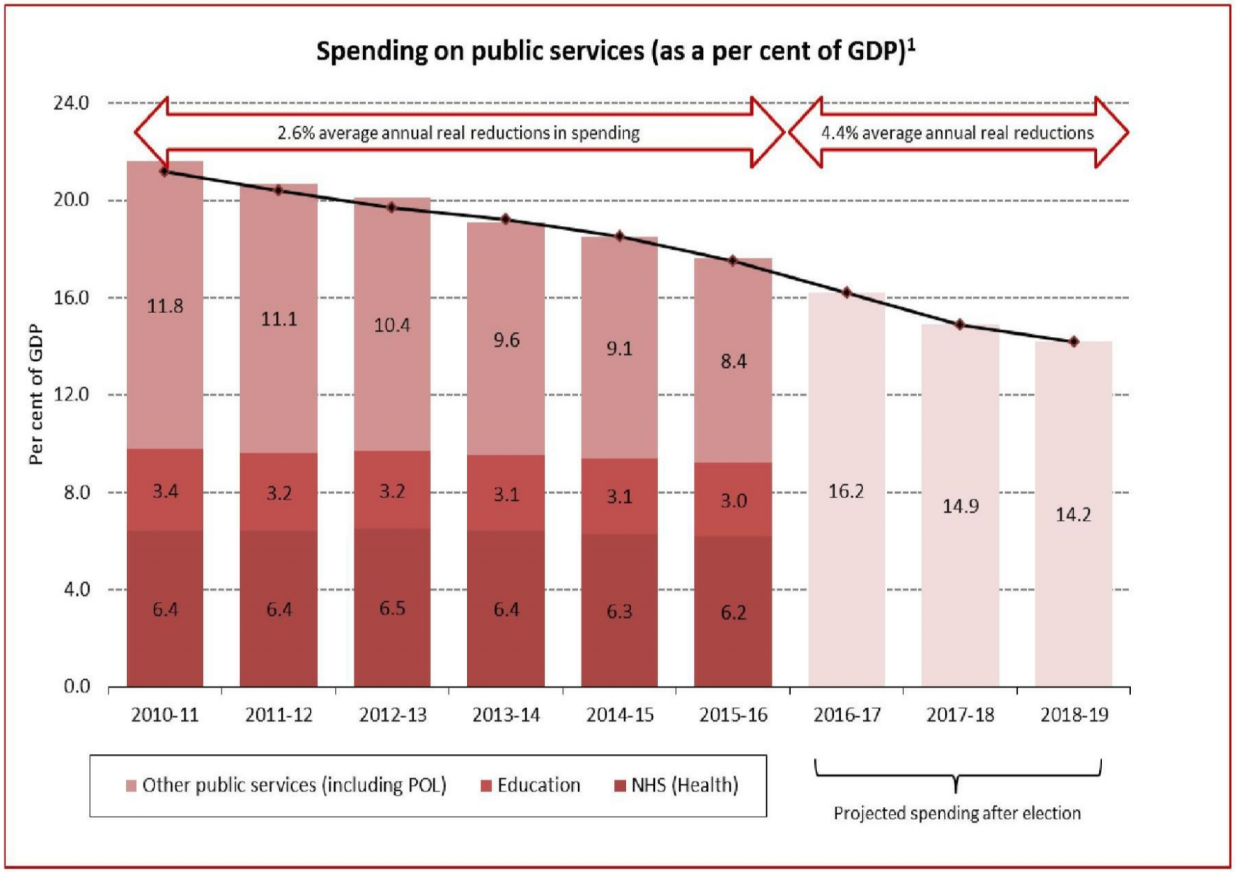
By targeting a £200-250m improvement in EBITDAS (relative to a 'do nothing' counterfactual), the Business Transformation Programme is seeking to close the gap to our Strategic Plan projections as far as possible, **but given the challenging market environment an adjustment to our financial flight path is likely to be necessary in almost all scenarios.**

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Nonetheless, given the political uncertainty and continued austerity expected after the next election, we need to continue working towards commercial sustainability as rapidly as possible

Key points on the public spending outlook:

- All of the main political parties have signalled a **continued tightening of the public finances after the next election**.
- With spending on health and education likely to be protected, other **departments like BIS face substantial cuts** – some estimates suggest by as much as 40-50% cumulatively between 2010/11 and 2018/19 (in real terms).
- And with BIS facing substantial challenges in other areas of its budget such as higher education, science and technology, this is likely to result in **strong pressure to reduce spending on the Post Office**.
- While our funding is fixed until 2017/18, **the incoming government will need to hold its next spending review (SR) by Autumn 2015** in order to set departmental budgets for at least 2016/17 – and it may choose to fix budgets up to 2018/19 or 2019/20 based on past experience.



- More generally, with polls suggesting an even closer result than the 2010 election, **the political uncertainty remains high**. A hung parliament is a strong likelihood, and media reports have suggested that senior civil servants are even considering the **prospect of two general elections in swift succession**, following the precedent set by Harold Wilson in 1974.
- Added to this uncertainty is the ongoing debate around **devolution of powers to Scotland and possibly other regions of the UK, which could potentially impact on the way the Post Office is funded**.

1. Source: Office of Budget Responsibility, March 2014 Economic and Fiscal Outlook. Assumes continuation of the Government's current overall fiscal mandate.

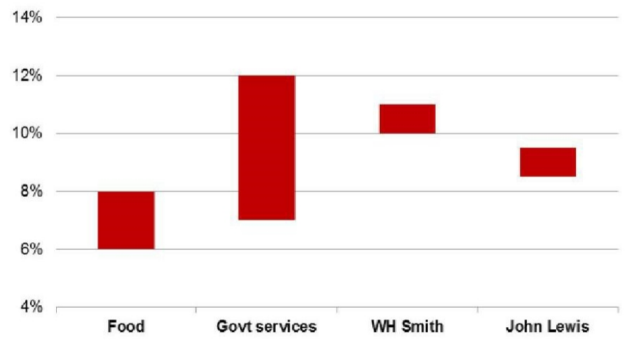
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Any recalibrated financial flight path must still meet some key success criteria to demonstrate progress towards sustainability

- While the pace of year-on-year improvements envisaged in the Strategic Plan may no longer be achievable, we would recommend that we should still be targeting a financial flight path that delivers the following key outcomes and milestones:
  - ✓ **No reopening of the existing funding settlement up to 2017/18**;
  - ✓ **EBITDAS run rate in March 2018 is consistent with a declining subsidy requirement in subsequent years** (off the baseline of £140m in 2017/18);
  - ✓ **Clear year-on-year improvements in EBITDAS throughout the plan period, with breakeven achieved by 2018/19 at the latest**; and
  - ✓ **By 2019/20 we should be meeting the characteristics of a financial independent organisation which we defined in our Strategic Plan** (see box on right hand side). Reaching that goal will also increase the prospect of us being viewed as 'bankable credit' by external investors, giving us more flexibility to pursue alternative financing in the absence of further HMG investment.
- Delivering these outcomes will ensure that we are not taking undue risks in our assumptions around the availability of HMG funding after 2017/18. And by continuing to make steady progress towards commercial sustainability, it should give us a better chance of securing the buy-in of key stakeholders to the turnaround.

Definition of financial independence: key criteria

1. A strategy and market position that allows us to compete effectively in our chosen markets – both now and in the future
2. The flexibility to respond quickly through corporate actions to unforeseen changes in these markets
3. An appropriate cost base and business model with the flexibility to withstand revenue volatility
4. A robust track record of profitability at an EBITDA margin in line with peers (typically 8-10% minimum in the retail sector – see chart below[1])
5. EBITDA margin not dependent on uncertain funding from HMG (so subsidy should either be much smaller or moved to long-term contract)
6. Sufficient free cash-flow to allow ongoing investment in the business to maintain commercial competitiveness in a continually evolving marketplace
7. Move to external financing of loan (not HMG) with quantum kept within affordable limits



Source: Rothschild; Food peer group includes

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We have modelled the financial sensitivity of different delivery outcomes using three scenarios: the first two scenarios represent the boundaries for our 'central planning range'

✓ Programme delivers impact

CENTRAL PLANNING RANGE

Scenario	Baseline performance	Reduce central costs	Reduce and variabilise network costs	Win in mails	Grow FS	Description
1. Full delivery, stable base	0% p.a.	✓	✓	✓	✓	• **Flat underlying business performance** • **All initiatives deliver in full (in line with the financial projections detailed in Appendix 1)**

2. Partial initiative delivery, stable base	0% p.a.	✓	✓	✓	✓	• **Flat underlying business performance**
						• **Commercial initiatives deliver partially:**
						  • Network Extension only serves to protect existing income (i.e. mails is flat rather than declining)
						  • FS reaches £460m in 19/20 (i.e. the 'medium' risks detailed in September strategy paper materialises)
						• **70% delivery of cost initiatives** due to execution risks

3. 'Do nothing' counter-factual	0% p.a.					• **Flat underlying business performance** • **Commercial initiatives do not deliver,** e.g., due to market conditions • **No cost initiatives deliver**, e.g. due to lack of political support

Source: Stage 3 baseline and programme financial charters

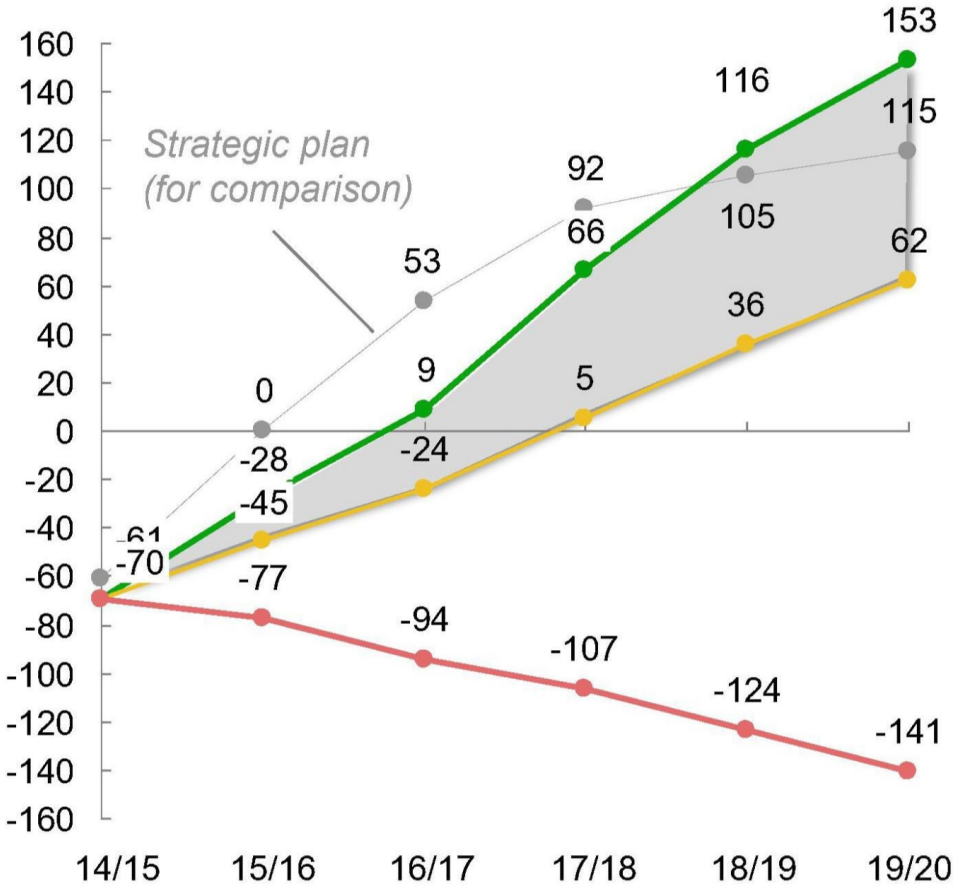
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These scenarios show that our central planning range meets the proposed criteria for an adjusted financial flight path

It should be noted that these figures exclude any payment for social provision but do carry the cost of the community branches

£m

EBITDAS exit run-rate



Scenario	Net income	Cost	EBITDAS
1. Full delivery, stable base	1,142	989	153
2. Partial initiative delivery, stable base	1,073	1,011	62
3. 'Do nothing' counter-factual	924	1,065	-141

2019/20 exit run-rate performance

✓ *Meets the criteria for adjusted financial flight path set out in slide 20*

✓ *Largely delivers criteria, but may need another year to demonstrate track record of commercial sustainability*

✗ *Fails to meet criteria – subsidy would have to increase and/or facing managed decline*

This has been constructed assuming a flat revenue profile beyond 2014/15 with central costs increasing in line with inflation and then layering in the impact of each programme initiative to 2019/20 (see appendix for details of each initiative)

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We have adjusted the programme funding requirements to keep within our existing envelope - but with the headroom falling within £200m by 2017/18 our scope to absorb new risks/priorities is limited

	2015 / 16	2016 / 17	2017 / 18	2018 / 19	2019 / 20
Available funding:					
Government funding	280	220	140	60*	50*
Total cumulative funding envelope (incl cash reserves)[1]	**929**	**1,052**	**1,188**	**1,281**	**1,394**
Required funding					
Total cumulative programme funding	380	706	858	904	945
Other essential capex (cumulative)[2]	30	60	100	150	200
Total cumulative funding needs	**410**	**766**	**958**	**1,054**	**1,145**
Headroom against funding envelope	**519**	**286**	**230**	**227**	**249**

1 – Balance sheet modeling assumes the bottom end of our EBITDAS planning range as set out on slide 22. *Also assumes £60m/£50m of HMG funding in 2018/19 and 2019/20, as per 2013 Strategic Plan assumptions. 2 – Provision for other essential capex and change costs (estimated).

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While we don't believe we need to reopen the existing funding settlement, we may need to explore alternative options for financing investment after 2017/18 if free cash flow insufficient

Option:	Potential quantum:	Considerations:
1. Seek additional funding from Government after 2017/18	• Could request £70m pa in 2018/19 and 2019/20 on top of £60/50m NSP already forecast while still delivering c10% pa reduction in total subsidy	• Dependent on wider pressures on BIS spending settlement, which are likely to be significant
2. Seek a loan (rather than grant) from Government to support transitional investment needs	• Depends on affordability within BIS capital budget – potentially £50-200m	• May be preferable fiscally for government as lending would not directly impact target to balance the current budget. • Would still count as state aid (calculated as the subsidy implicit in the interest rate compared with private sector lending) – but European Commission may view the whole loan amount as subsidy if they believe there is a high chance of it being written off
3. Seek bank/external financing	• Currently constrained by BIS to £50m of external borrowing and £50m in finance leases – but could seek to increase those limits	• Financing only likely to be forthcoming if we're seen as 'bankable credit' (see definition of financial independence in earlier slide) or there is an asset/income stream against which the loan can be secured – or if the banks believe there is an implicit guarantee from HMG. • Alternatively we could seek an explicit guarantee from government but this would be viewed as state aid (and vfm for taxpayer is poorer than a direct loan but with the same credit exposure)
4. Seek partner financing (e.g. from Royal Mail or BoI)	• Unlikely to be substantial	• Not currently assumed to be a lead option – would require much closer commercial alignment with our key partners
5. Asset disposals	• Limited assets available for disposal. Most significant standalone option is to dispose of the HPBB business - could potentially release c£40m	• Options to be managed as part of ongoing strategic portfolio management – see separate slide deck on 'Levers for adjusting our strategy to respond to new risks and opportunities'

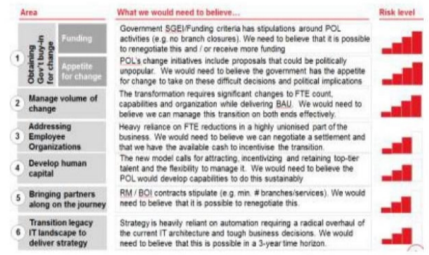
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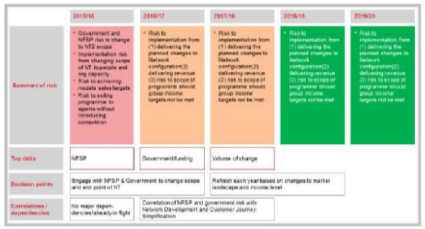
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Programme delivery risks have been assessed bottom-up using a 4-step methodology



Step 1

We defined 'need-to-be-true' criteria and mapped these to programmes



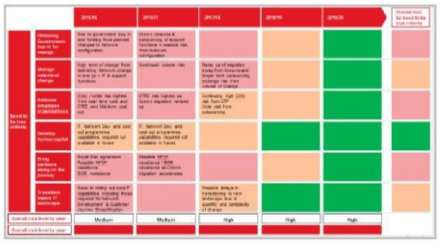
Step 2

We worked with each programme owner to map risks over time, identifying decision points and dependencies / correlations



Step 3

A consolidated risk "heat map" by programme, by theme, and by year was developed, illustrating that year one will be "make-it-or-break-it", and that risk is highest for revenue growth initiatives (outside of our control).



Step 4

An alternative lens – mapping risk by needs to be true criteria over time to enable integrated risk mitigation planning, e.g:

- Engaging employee organisations
- Securing Gov' buy-in
- Negotiating with commercial partners
- Designing IT roadmap
- Developing human capital
- Establishing robust change management

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Programme delivery risk mitigations include central governance/control, operational planning, and testing external dependencies early to avoid stranded costs

Theme	Risk of non-delivery	Specific risks
Reduce central costs Transform the organisation Lean IT	Moderate	• CWU or Unite industrial action • Outsource partner issues in design and transition
Reduce and variabilise network costs	High	• CWU industrial action • NFSP resists agent pay renegotiation • Royal Mail blocks customer journey simplification • Dependency of technology delivery partners
Grow Financial Services	High	• Bank of Ireland unwilling to accept changes • Existing exclusivity arrangement precludes pursuing other opportunities
Win in Mails	High	• NFSP blocks Network Development • Royal Mail blocks Network Development • Some initiatives not yet fully planned

Overall risks

- Lack of capacity and capability to manage the volume and complexity of change without disrupting BAU performance
- CWU / NFSP pressure disrupts BAU performance and/or undermines public and government good will
- Government unwilling to support radical outcomes of combined initiatives
- Delay / failure in technology enablement and delivery leads to business caught in 'no-mans' land
- Market pressures lead to demand for further strategic initiatives to be delivered on top of existing stretching plan – accelerate portfolio diversification to drive revenue growth

Approach to managing risk

- **Prioritise cost out initiatives, which have fewer external dependencies than revenue growth**
- **Ensure strong execution using appropriate partners**
- **Avoid "stranded investment"** by developing operational plans and testing external dependencies early
- **Track and assess delivery and course correct**, by setting up strong central governance
- **Ultimately if transformation impact is not possible then need to consider alternative strategic levers to deliver required EBITDAS performance – slide 30**

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In addition to delivery risk, there are a number of reputational and operational risks that could impact our customers

Risk	Risk level	Mitigation actions
Combination of media, CWU, NFSP, local campaigns impact government	High; no way to fully mitigate	Put in place a robust stakeholder management plan, monitor reaction and course correct
High volume of change results in degradation in BAU performance	High if not properly managed, due to high volume of changes to products, processes and organisation structure being driven by multiple initiatives	Establish central control/governance to coordinate and communicate change for front line Ensure clear operational delivery plans, risk assessments and risk mitigations in place for each initiative before embarking Organise front line change into coordinated waves
Customers lose goodwill due to perception that Post Office actions are not in line with customer values	High if not properly planned for, due to potential customer perceptions accentuated by media dialogue, industrial action and political debate	Develop and action clear customer communication plans showing how actions help Post Office stay relevant to customers (e.g., by creating a more convenient branch network, better value products, and faster parcel drop-off)
IT system transitions result in temporary loss of critical services	High if transitions not properly managed due to complex landscape of legacy systems and changing vendors	Use experienced partners, ensure extensive testing and pilots, and structure KPIs into vendor contract
Customers react negatively to multi-format network	Low; strong programme governance and improved Network will minimise residual risk level	Drive customer communications with clearly differentiated brand and proposition for access points, and emphasise service and convenience
Potential knowledge loss when employees exit	Low; appropriate preparedness by teams can mitigate risk level	Each function to develop knowledge retention plans ahead of any wave of exits

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We also face the threat of disintermediation, which arguably represents the biggest long-term risk to our business model

- While our business model has some intrinsic strengths, the fact that most of our products are sourced wholesale from single upstream suppliers leaves us **exposed to the risk of gradual (and possibly abrupt) disintermediation.**
- **This is particularly the case in mails**. Separation from Royal Mail has its advantages, but it has also cemented our status as a retail intermediary. There are no precedents for this split amongst other major national postal services, and so the long-term consequences are uncertain – particularly during a period when **new competitors and technologies are disrupting the traditional B2C (and C2C) parcels fulfilment model**.
- **These risks need to be central to our strategic considerations** - there are some clear lessons for us from the Phones 4u experience as set out below.

Case study: five lessons from the Phones 4U experience

In September Phones 4u – a business with 5,500 employees, 720 outlets and £1bn of turnover generating EBITDA of £105m last year – was pushed into administration by the withdrawal of its last two major suppliers, EE and Vodafone, leaving it with no real business. While the collapse was sudden, the market shifts which led to it were gradual but seemingly unforeseen by the management and owner. There are five key insights we can extract from this episode:

1. **Adjust to changing consumer trends** – Phones 4u's business model was built on the fact that in the early days of the mobile market customers needed a trusted intermediary to provide advice on the bewildering choice of tariff structures and handsets from different providers. But customers have become much savvier over time and there is now less demand for this type of role. There are clear parallels in the way the parcels market is developing.
2. **Beware of your suppliers developing their own channels** – linked to this last point, a decade ago the network operators were disinclined to invest in their own sales structures, but with declining margins in the industry over recent years they have become less willing to pay commission to a third party. As a consequence they now have over 2,000 retail outlets of their own and are also investing heavily in their online capabilities.
3. **Protect and invest in your source of added value** – Phones 4U failed to keep investing in its network and capabilities to give it a differentiated proposition in an increasingly crowded market. To survive as an intermediary you need to be clear on your USP - in our case it's a combination of our relationships with host retailers, our ability to source products from a range of areas (mails, FS, government and home services) and our IT interfaces (either existing or under development). These attributes are not easily replicated, and thus provide 'barriers to disintermediation' – but they are certainly not impossible to circumvent.
4. **Financial flexibility is essential to survive in a low margin environment** – Phones 4u's debt burden, equivalent to four times EBITDA, left them with limited wriggle room to renegotiate terms with suppliers. The equivalent burden in our case is our legacy of high fixed costs which if not tackled will limit our ability to cope with margin squeeze by suppliers in the future. There is no long-term role for an expensive intermediary in a highly competitive market.
5. **Income diversification can help offset supplier risks** – Phones 4u was almost entirely dependent on the revenue derived from its suppliers, having sold an insurance subsidiary (Lifestyle Services Group) last year that had offered a degree of income diversification. Our revenue base is more diversified and building greater ownership of the value chain in areas such as insurance will further reduce our dependence on major suppliers.

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We will use three broad levers to adjust our strategy to respond to these various risks and challenges as they arise

	Description:	Considerations for use:
1 Work with other partners	• Explore working with other delivery partners and/or upstream retail clients in addition to Royal Mail • We have less single-partner risk within FS, although BoI is clearly critical to our growth plans in certain products. The options here are explored in the separate Board paper.	• Breaking exclusivity with RM would be a significant step with major legal (and operational) hurdles – would only be appropriate to consider if it is clear that we can't achieve adequate commercial alignment and/or their own market share is under severe pressure.
2 Further cost out and channel shift	• Proposed TOM already envisages a substantial shift in the network mix, but scope to adjust the balance between different operating models depending on market dynamics. • We could potentially focus more of our investment on the digital/direct business if branches underperform. • We're reviewing options to reconfigure cash intensive products more proactively to reduce supply chain demand	• In a low income growth scenario we would most likely roll out fewer new access points and 'Local Lights' to avoid spreading income too thinly. The Mains would become more dependent on host retail to remain viable, and it would also potentially strengthen the case for accelerating Crowns divestment and managing supply chain demand more aggressively. • Longer-term there may also be potential for further recalibration of agents pay in line with market rates – but dependent on achieving product simplification and network reconfiguration first
3 Strategic portfolio management	• Covers a range of measures to either accelerate growth or withdraw from areas which are not closely aligned with core strategy. Could include acquisitions in profitable areas or divestments to release capital and capacity. • Need to particularly focus on options which could make our offer to host retailers more attractive versus the competition .	• Active portfolio management should be an ongoing part of our strategy under any scenario, but becomes increasingly important if current income growth assumptions do not materialise as planned and we're losing ground to competitors.

These levers are explored in more detail in Appendix 3

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The transformation will require strong, central governance and control to ensure the value is delivered

Characteristics of POL transformation: Uncertain outcome and significant cross functional dependency

- **Detailed target state design needed** for each programme
- **Complex cross-functional linkages** across channels, products, operations, IT, people and engagement
- **Constrained management capacity and funding**
- **Mixed change capability** with variable heritage (staff/ contractor mix)
- **Uncertain outcome** depending on external stakeholders and market conditions

Need strong central governance and TMO to…

- **Challenge programme leads to ensure the design and delivery focuses on capturing the value leveraging 'Enterprise Design Authority'**
- **Manage across functions and programmes**
  - **Ensure the design is joined up**
  - **Identify issues and mobilise functions** to work together
  - **Create integrated view of benefits tracking, issues and risks**
  - **Escalate tough decisions** to ExCo
- **"Own" overall change sourcing, funding and dynamically manage portfolio** to prioritise funding and capacity
- **Oversee sourcing of the right partners** for successful delivery and **provide "SWAT team"** to remediate failing initiatives
- **Prompt strategic changes in the plan** to respond to external events

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Proposed governance and controls

The proposed structure to support Transformation is summarised in the following pages:

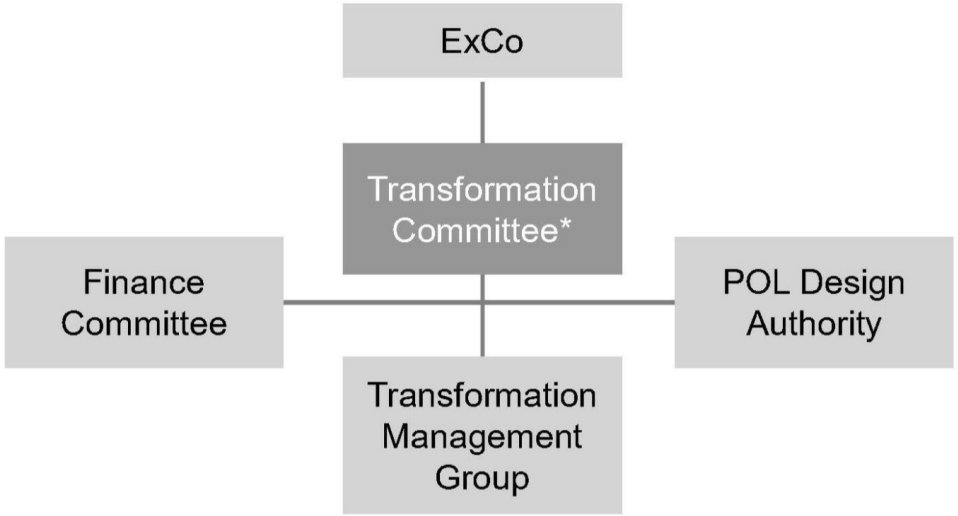
The structure (Roles and responsibilities, Reporting, Terms of Reference) will be reviewed during the transition phase and aligned with the other POL governance bodies

In addition we propose to:

1. Establish and populate a POL Design Authority (Business/Technology)
2. Establish and populate a Transformation Management Group
3. Accelerate the development of a Transformation Management Office to provide effective portfolio management of the Transformation delivery led by the Transformation Director
4. Accelerate the development of the risk/assurance function to support the TMO to manage the Transformation delivery led by the Director of Corporate Services
5. Cluster relevant programmes under individual Ex-Co sponsors to create single accountability and ownership for delivery of outcomes and benefits

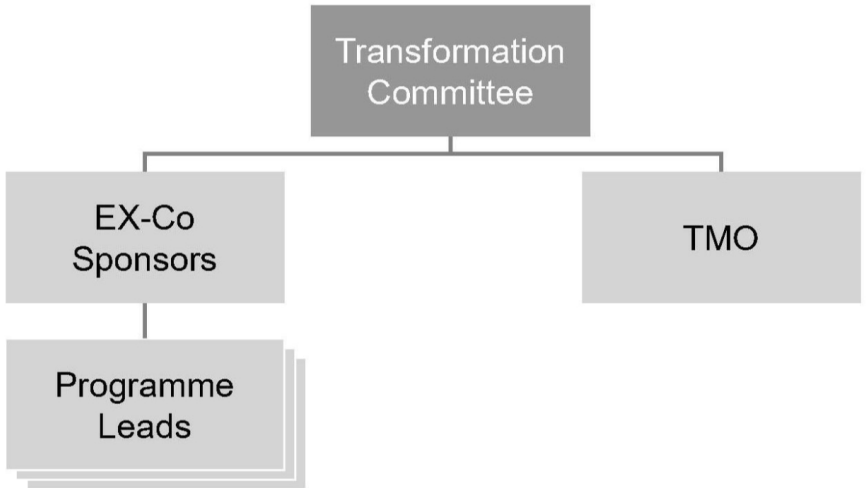
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Proposed governance and controls



* See below for detail

- Transformation Committee – manages delivery and course correction to manage risk
- Finance Committee – review and challenge to requests for funding prior to submission to TC for approval
- POL Design Authority owns 'end state' design and transition states. Provides first line review for all initiatives to confirm alignment with target state
- Transformation Management Group – day-to-day management of Transformation Portfolios



- Ex-Co Sponsors – accountable for programme outcomes and benefits
- Programme Leads (Director/Manager) – responsible for delivery of programmes consistent with agreed Terms of Reference
- TMO – responsible for overall transformation portfolio management and related activities (Business case, Benefits, Assurance, Sourcing, Reporting, Change Management)

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The next few months will focus on putting in place the critical success factors for transformation implementation

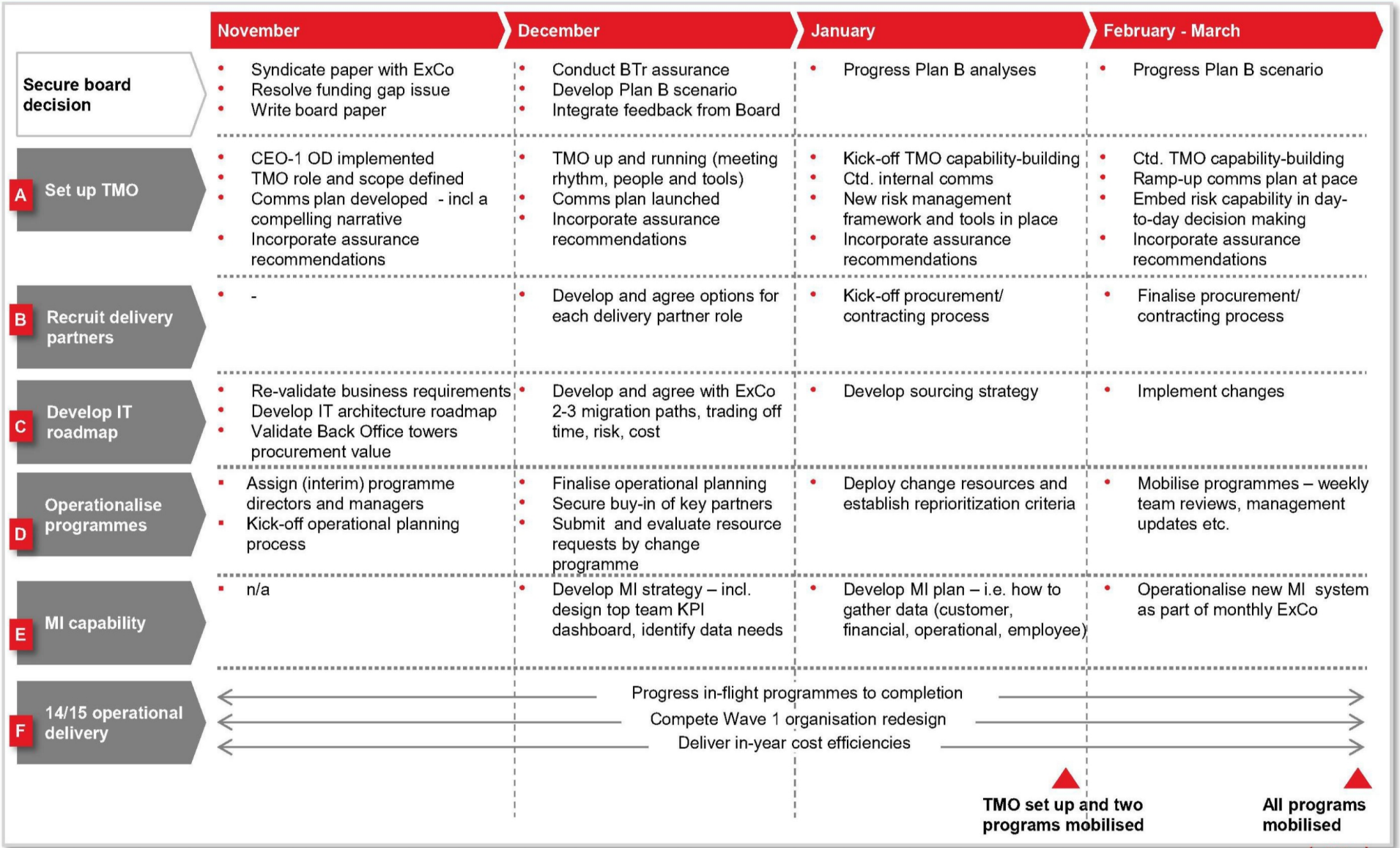
- ✓ **A. Strong central governance supported by a CTO and TMO accountable for ensuring the value is delivered across the whole transformation**
- ✓ **B. Appropriate partners in place** by adjusting existing contracts or contracting new partners
- ✓ **C. Credible record of operational delivery by delivering in-year cost efficiency** in H2 2014/15 and strong compelling change narrative in place
- ✓ **D. Robust IT roadmap** describing what transformation programmes need from IT in order to deliver their targets, architecture roadmap to deliver this, and partner strategy for delivering
- ✓ **E. Programmes operational and pre-launch success criteria met:** Teams mobilised and operational plans developed and analysed to assess impact on risk and interdependencies
- ✓ **F. MI capability** to track business / programme performance and enable effective decision-making

…in addition to alignment of the Executive team, Board support and assurance from completing the assurance review of Business Transformation outputs from stage II and III, and securing Board support for the proposed way forward

Activity and milestones for the above will be tracked by Transformation Committee

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Parallel streams of activity are required to transition to delivery, whilst addressing the "entry criteria"



	November	December	January	February - March
Secure board decision	• Syndicate paper with ExCo • Resolve funding gap issue • Write board paper	• Conduct BTr assurance • Develop Plan B scenario • Integrate feedback from Board	• Progress Plan B analyses	• Progress Plan B scenario
A Set up TMO	• CEO-1 OD implemented • TMO role and scope defined • Comms plan developed - incl a compelling narrative • Incorporate assurance recommendations	• TMO up and running (meeting rhythm, people and tools) • Comms plan launched • Incorporate assurance recommendations	• Kick-off TMO capability-building • Ctd. internal comms • New risk management framework and tools in place • Incorporate assurance recommendations	• Ctd. TMO capability-building • Ramp-up comms plan at pace • Embed risk capability in day-to-day decision making • Incorporate assurance recommendations
B Recruit delivery partners	• -	• Develop and agree options for each delivery partner role	• Kick-off procurement/ contracting process	• Finalise procurement/ contracting process
C Develop IT roadmap	• Re-validate business requirements • Develop IT architecture roadmap • Validate Back Office towers procurement value	• Develop and agree with ExCo 2-3 migration paths, trading off time, risk, cost	• Develop sourcing strategy	• Implement changes
D Operationalise programmes	• Assign (interim) programme directors and managers • Kick-off operational planning process	• Finalise operational planning • Secure buy-in of key partners • Submit and evaluate resource requests by change programme	• Deploy change resources and establish reprioritization criteria	• Mobilise programmes – weekly team reviews, management updates etc.
E MI capability	• n/a	• Develop MI strategy – incl. design top team KPI dashboard, identify data needs	• Develop MI plan – i.e. how to gather data (customer, financial, operational, employee)	• Operationalise new MI system as part of monthly ExCo
F 14/15 operational delivery	Progress in-flight programmes to completion Compete Wave 1 organisation redesign Deliver in-year cost efficiencies			

TMO set up and two programs mobilised

All programs mobilised

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We anticipate four types of third party partner support will be required to assist with the transformation journey

Design partners			
Transformation management partner	**Detailed design partner**	**Implementation and outsourcing partners**	**Assurance partner**
▪ Ensures delivery against targets ▪ Defines value drivers and KPIs for each initiative ▪ Mobilises teams and ensures appropriate partners ▪ Ensures designs are joined up across programmes ▪ Escalates issues and drives tough ExCo decisions ▪ Manages internal communications ▪ Delivers proactive "SWAT team support" to delivery teams ▪ Prompts changes in the plan to respond to external events	▪ Designs detailed end state and execution plan for targeted initiatives ▪ Drives ExCo to make tough decisions ▪ Brings targeted expertise (e.g., cloud HR solution choice)	▪ Drives change once end state and plan agreed ▪ Optionally runs function if needed ▪ Brings implementation expertise (e.g., lean), capacity, and scale	▪ Assures programme and value delivery ▪ Provides independent line of defence in risk management ▪ Deliver key checkpoint assurance and deep dive reviews

Separation between design partners and implementation/outsourcing partners helps optimise capabilities and economics, ensure clear accountability, and avoid conflict of interest

We will select the key partners to assist with the transformation during the transition phase

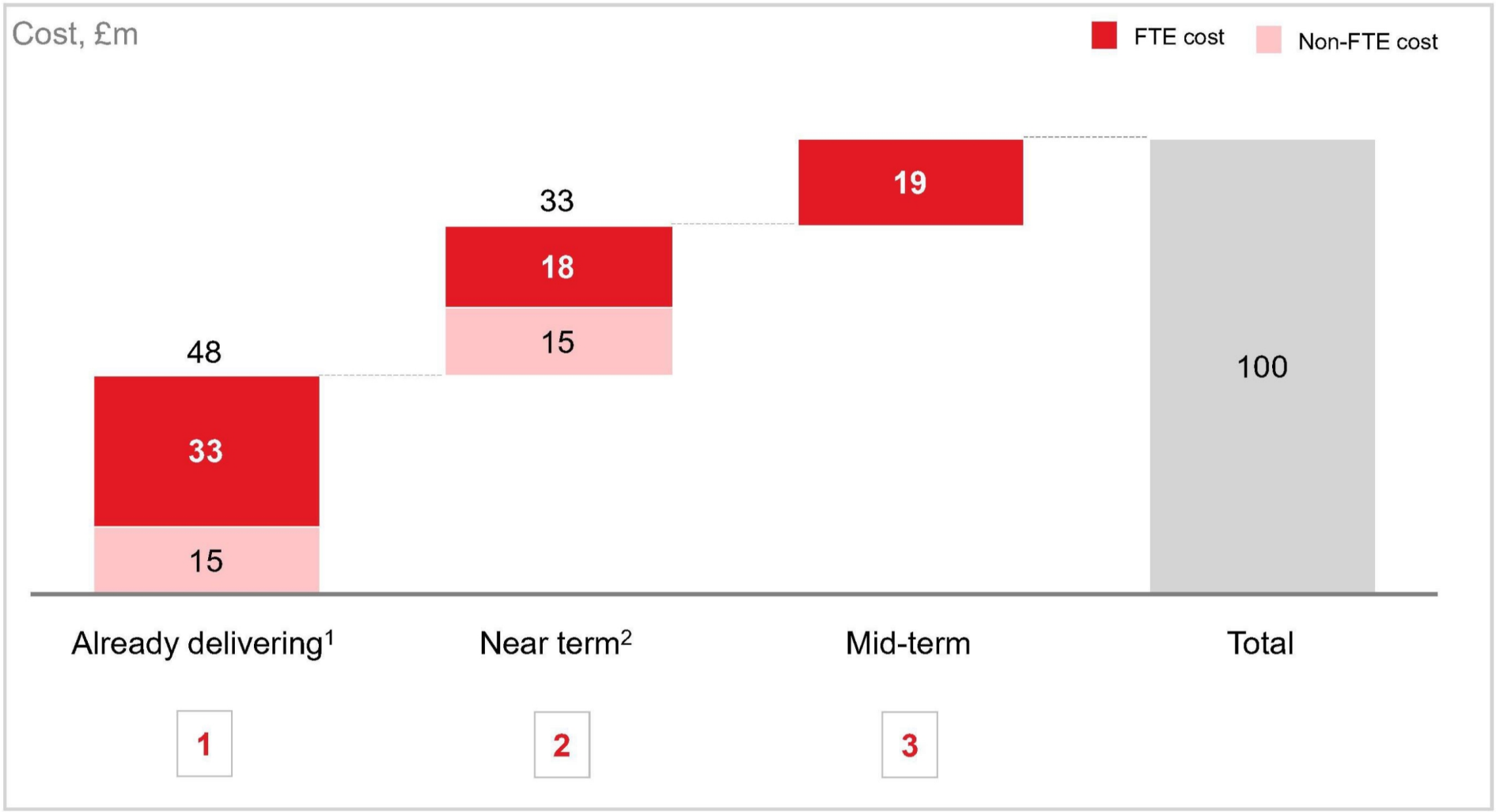
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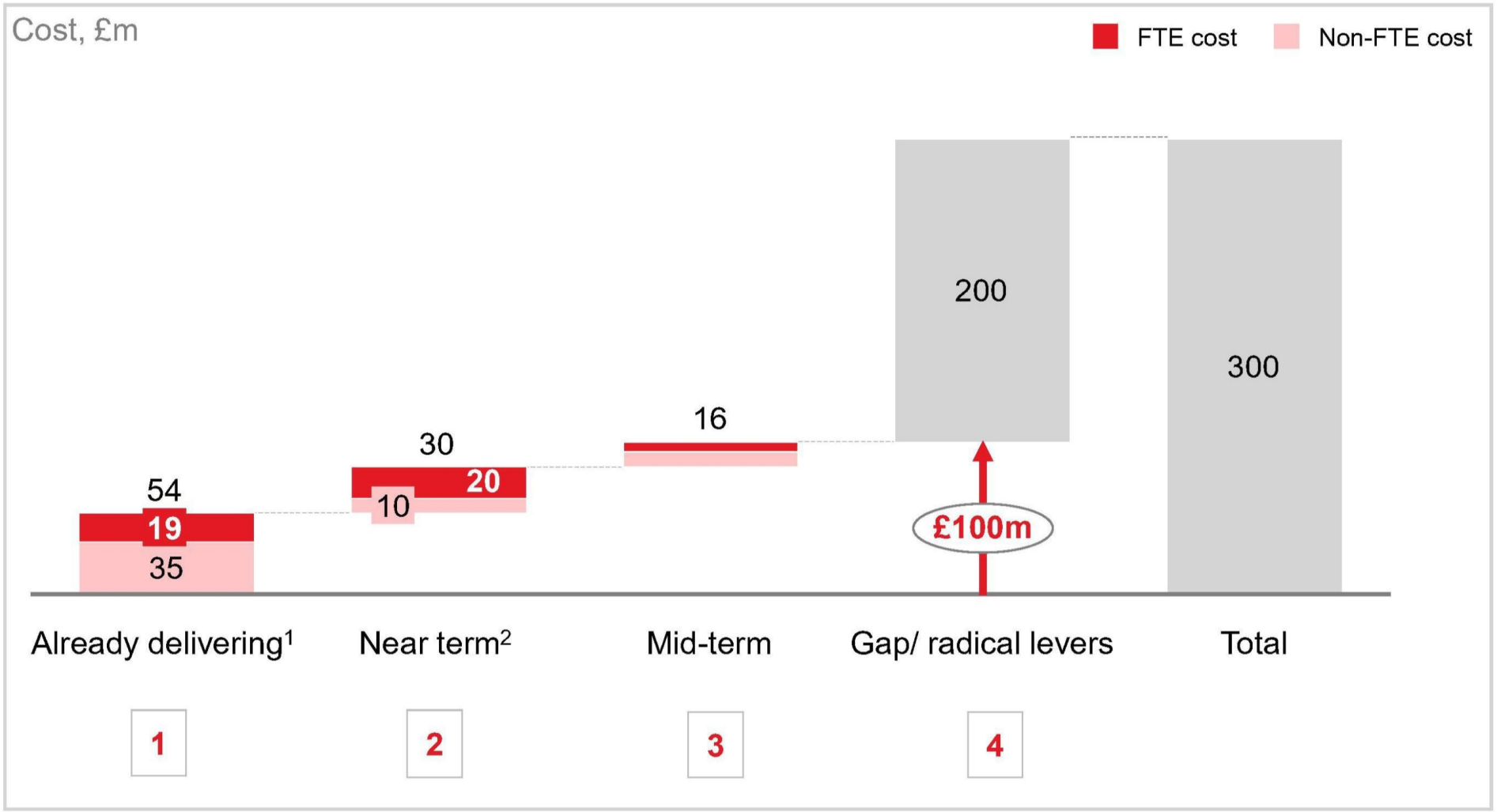
Stage 1 output (4 August) identified £100m of near and mid-term central cost saving



1 BAU only, excluding BTLI – FY15/16 run-rate
2 Already delivering initiatives de-duplicated

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We are expecting to over deliver 15/16 run rate from 14/15 initiatives and have line of sight to deliver at least £100m by March 2016



1 BAU only, excluding BTLI – FY15/16 run-rate
2 Already delivering initiatives de-duplicated

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Progress in Financial Year 2014/15

- We are currently reporting (as at week commencing 17th November 2014) central cost savings of IRRELEVANT in FY 14/15 as per the table below.
- This equates to IRRELEVANT of recurring annualised cost saving. The baseline already included IRRELEVANT of savings that were committed to before June 2014 and therefore the total "on-track" annualised cost saving above baseline is IRRELEVANT
- We have line of sight to a further IRRELEVANT of in-year opportunities and cross functional options for cost saving, the majority of which are one-off in year savings but also include c. IRRELEVANT of recurring cost reduction opportunities. For the latest target we have risk adjusted down t IRRELEVANT
- The total expected recurring saving to the 2014 baseline from in-year activity is **IRRELEVANT**

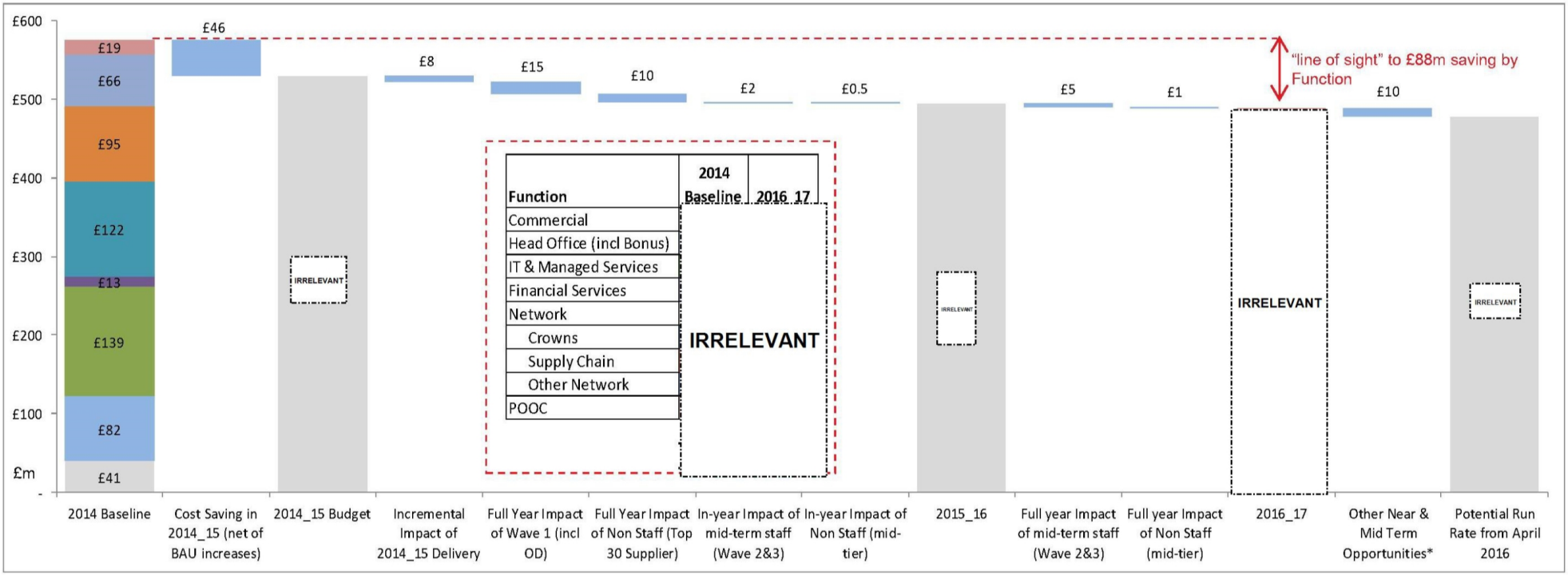
Functional Area	Owner	Revised Target	Green	Delivered	Total "On-Track"	Gap to Target
Commercial	Martin George					
Commercial - POOC	*Martin George*					
Finance	Chris Day					
Financial Services	Nick Kennett					
FS - POOC	*Nick Kennett*					
People & Engagement	Neil Hayward					
Corporate Services	Chris Aujard					
Network	Kevin Gilliland					
IT / Technology	Lesley Sewell					
Total						

IRRELEVANT

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Illustrative potential impact on central cost base to March 2016 (Staff, Non-staff and POOC) – final position to be confirmed

- Shows expected split by Function from the June 2014 baseline to 16_17 plus additional potential cross functional savings
- Excludes incremental cost of growth in Commercial and Financial Services
- Split by function is **directional** and doesn't represent budgets or targets at this stage
- The initial 2015_16 budget target set is slightly more aggressive and aims to build in £100m saving to the 2015_16 budget



*Other potential near & mid term opportunities from the following (excludes in-year 16/17 savings from outsourcing);

1) Semi-automation across the business (c. £2m)
2) Strategy for Swindon (c. £2m)
3) Optimise customer service journey (c. £2m)
4) VAT vs NI on Agents pay (c. £4m +)
5) Product rationalisation (c. £3m)
6) Contractual adherence on volume based contracts (£tbc)
7) Staff wave 1 and OD – identified £16m but only £15m taken above (£1m) (£5m)
8) Supplier engagement process - identified £15m only £10m taken above

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IT investment required to deliver our business outcomes is spread across a number of programmes

Theme	Programme	Incremental IT funding costs, £m	IT requirements
Reduce central costs	1a: Near-term cost out	-	▪ No IT impact
	1b: Finance/HR transformation	15.0	▪ Maintain system resilience until outsourced ▪ Then move to BPO cloud-based services
	1c: Network Support transformation	-[2]	▪ Move to self service and automated processes
	1d: Long-term efficiencies	-[2]	▪ To be decided in 2016/17
Transform the organisation	2: OD & people development	-	▪ No IT impact
Lean IT	3: Lean IT	184.5	▪ £91m - Front Office migration from Horizon to CDP ▪ £41m - Branch counter refresh ▪ £20m - Towers procurement and transition ▪ £32.5m - IT enablers incl. integration, security, CDP
Reduce and variabilise network costs	4a: Network Transformation	N/A[1]	▪ Equipment and support for new branches
	4b: Crown Transformation 2	N/A[1]	▪ Equipment and network support for new Mains
	4c: Customer journey simplification	5.0	▪ Integration and implementation of simplified journeys
Win in mails	5a: Network Extension	14.5	▪ CDP, integration and branch counter equipment
	5b: Commercial strategy	17.5	▪ Data and analytics, CDP and integration
Grow FS	6: Financial Services strategy	32.5	▪ Data and analytics, CRM, CDP and integration
Total		269	

Early estimates based on outside-in view from IT team; being aligned with programme leads

2 Potential underestimate; programme financial charter allows for much greater investment
Source: Stage 3 programme financial charters

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Over £200m of the £1,143m funding capacity is related to digital channel development

Theme	Programme	Overall funding, £m	Funding related to digital channels, £m	Description of digital investment
Reduce central costs	1a: Near-term cost out	25	-	▪ N/A
	1b: Finance/HR transformation	15	-	▪ N/A
	1c: Network Support transformation	28	-	▪ N/A
	1d: Long-term efficiencies	45	-	▪ N/A
Transform the organisation	2: OD & people development	3	-	▪ N/A
Lean IT	3: Lean IT	185	124	▪ Horizon migration and IT enablers for digital
Reduce and variabilise network costs	4a: Network Transformation	445	-	▪ N/A
	4b: Crown Transformation 2	71	-	▪ N/A
	4c: Customer journey simplification	12	12	▪ Allow journeys to start online
Win in mails	5a: Network Extension	31	31	▪ Allow journeys to start online
	5b: Commercial strategy	19	19	▪ eCommerce and SME propositions
Grow FS	6: Financial Services strategy	36	36	▪ Integrated digital customer experience
Enablers	Establish transformation enablers incl. TMO	30	-	▪ N/A
Additional funding	Provision for other essential capex and change costs	200	-	▪ N/A
Total		**1,145**	**222**	

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SUBMITTING BY DIGITAL TEAM

Digitisation of our business is central to delivery of the plan

Digital Enablers

Processes transformed through digital first approach (transactions, comms and support)	Simplified product journeys (based on knowledge of customers) and increased use of self-serve in online channels and in-store	Increased focus on online revenue generation through capability development and marketing optimisation	Creation of rich data set around customers and operations

Outcomes

Reduction in FTE (central) Reduction in transaction times/agent pay Reduced central costs Data sets	Increased customer satisfaction Reduction in queues Reduced attrition	Increased channel contribution (income).	Increased marketing efficiency. Operational improvements New income opportunities

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Contents

- Strategic context and target operating model
- Roadmap
- Analysis of financial impact
- Risk and mitigation
- Governance and controls
- Transition plan and partners
- Plan for near-term cost out to 15/16
- Appendix: Technology and digital
- **Appendix: Additional financials**

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PRELIMINARY

Baseline scenario

	2014/15 P6 forecast	2015/16	2016/17	2017/18	2018/19	2019/20
Net Income	IRRELEVANT					
Central costs						
Supply Chain						
Crowns						
Other Network						
IT						
Commercial						
Financial Serv						
Support Func						
POOC						
Total central costs						
Agents' Pay						
Total costs						
EBITDAS						

Assumptions

- Pillar income remains flat at £IRRELEVANT P6 forecast
- SC and other income increases from IRRELEVANT to IRRELEVANT as per June Board presentation
- Central costs increase with inflation
- Agent pay stays flat

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Backup: We plan to achieve a ~30% reduction in central costs by 2019/20

Cost, £m

	In year savings by end 14/15	14/15 P6 outlook, incl. in-year savings	Inflation uplift to 19/20	19/20 baseline after inflation (c. 2.5%)	Impact of cost out by end 19/20	19/20 baseline after cost out	Impact in cost of income growth by end 19/20	19/20 after cost out and income growth
Central costs								
Supply Chain								
Crowns								
Other Network								
IT								
Commercial								
Financial Services								
Support Func								
POOC								
Not yet allocated[1]								
Total central costs								
Agents' Pay								
Total costs								

IRRELEVANT

~30% reduction in central costs, driven by:

- **£146m reduction** from cost out initiatives
- **£54m in year savings in 14/15** already factored into baseline

1 Additional £12m in 19/20 terms will be driven out by initiatives currently being scoped within programme 1a including review of stock supply chain, product rationalisation, and VAT/NI review

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INITIAL ESTIMATE - SUBJECT TO REFINEMENT

Net income glidepath by programme

Net income, £m

Area	Baseline scenario	2015 / 16	2016 / 17	2017 / 18	2018 / 19	2019 / 20
	Baseline scenario	**915**	**921**	**920**	**924**	**924**
Reduce central costs	1a Near-term cost out	0	0	0	0	0
	1b Finance/HR transformation	0	0	0	0	0
	1c Network Support transformation	0	0	0	0	0
	1d Long-term efficiencies	0	0	0	0	0
Transform the organisation	2 OD & People	0	0	0	0	0
Lean IT	3 Lean IT	0	0	0	0	0
Reduce and variabilise network costs	4a Network Transformation	0	0	0	0	0
	4b Crown Transformation 2	-1	-4	-5	-7	-8
	4c Customer journey simplification	0	0	-4	-19	-30
Win in mails	5a Network Extension	5	17	27	29	32
	5b Commercial strategy	5	16	32	48	48
Grow FS	6 Grow FS	27	57	117	152	177
Enablers	Establish transformation enablers incl. TMO	0	0	0	0	0
Total		**956**	**1,005**	**1,090**	**1,127**	**1,142**

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Source: Stage 3 programme financial charters

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INITIAL ESTIMATE - SUBJECT TO REFINEMENT

Cost glidepath by programme

Cost, £m

Area	Baseline scenario	2015 / 16	2016 / 17	2017 / 18	2018 / 19	2019 / 20
	Baseline scenario	**-998**	**-1,014**	**-1,031**	**-1,048**	**-1,065**
Reduce central costs	1a Near-term cost out	45	46	47	48	50
	1b Finance/HR transformation	0	4	4	4	4
	1c Network Support transformation	0	7	7	7	8
	1d Long-term efficiencies	0	0	6	11	17
Transform the organisation	2 OD & People	0	0	0	0	0
Lean IT	3 Lean IT	-3	-9	3	9	22
Reduce and variabilise network costs	4a Network Transformation	11	22	31	35	35
	4b Crown Transformation 2	4	11	17	21	24
	4c Customer journey simplification	0	0	8	39	61
Win in mails	5a Network Extension	-9	-18	-24	-25	-26
	5b Commercial strategy	-4	-13	-26	-38	-38
Grow FS	6 Grow FS	-30	-33	-66	-75	-80
Enablers	Establish transformation enablers incl. TMO	-	-	-	-	-
Total		**-984**	**-997**	**-1,024**	**-1,011**	**-989**

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Source: Stage 3 programme financial charters

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INITIAL ESTIMATE - SUBJECT TO REFINEMENT

EBITDAS glidepath by programme

Net income, £m

Area	Baseline scenario	2015 / 16	2016 / 17	2017 / 18	2018 / 19	2019 / 20
		-77	-94	-107	-124	-141
Reduce central costs	1a Near-term cost out	45	46	47	48	50
	1b Finance/HR transformation	0	4	4	4	4
	1c Network Support transformation	0	7	7	7	8
	1d Long-term efficiencies	0	0	6	11	17
Transform the organisation	2 OD & People	0	0	0	0	0
Lean IT	3 Lean IT	-3	-9	3	9	22
Reduce and variabilise network costs	4a Network Transformation	11	22	31	35	35
	4b Crown Transformation 2	3	7	11	14	16
	4c Customer journey simplification	0	0	4	19	30
Win in mails	5a Network Extension	-4	-2	3	5	6
	5b Commercial strategy	1	3	6	10	10
Grow FS	6 Grow FS	-3	23	50	78	97
Enablers	Establish transformation enablers incl. TMO	-	-	-	-	-
Total		-28	9	66	116	153

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Source: Stage 3 programme financial charters

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INITIAL ESTIMATE - SUBJECT TO REFINEMENT

Funding glidepath by programme

Funding, £m

Area		2015 / 16	2016 / 17	2017 / 18	2018 / 19	2019 / 20
	Baseline scenario	**30**	**30**	**40**	**50**	**50**
Reduce central costs	1a Near-term cost out	18	7	0	0	0
	1b Finance/HR transformation	8	8	0	0	0
	1c Network Support transformation	14	14	0	0	0
	1d Long-term efficiencies	0	0	15	15	15
Transform the organisation	2 OD & People	1	1	0	0	0
Lean IT	3 Lean IT	84	71	29	0	0
Reduce and variabilise network costs	4a Network Transformation	196	161	64	14	11
	4b Crown Transformation 2	13	22	17	11	7
	4c Customer journey simplification	6	2	4	0	0
Win in mails	5a Network Extension	16	13	1	0	0
	5b Commercial strategy	0	6	10	2	2
Grow FS	6 Grow FS	15	11	4	3	3
Enablers	Establish transformation enablers incl. TMO	9	9	9	1	1
Total		**410**	**356**	**192**	**96**	**89**

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Source: Stage 3 programme financial charters

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POST OFFICE LTD BOARD

PwC review of the transformation programme

1. Purpose

The purpose of this paper is to request the Board to note the accompanying review paper from PwC on the Business Transformation Programme ("BTP").

2. Background and context

With a view to assisting the Board in its consideration of the matters set out in the Board Paper by David Ryan entitled "Business Transformation Programme", due to be considered at this November meeting, (the "David Ryan paper"), PwC were engaged in late October to undertake a short and focussed independent review of certain aspects of the work of, and recommendations made by, the BTP team. It was acknowledged by all parties at the inception of PwC's engagement that, given both the extremely tight time scales and the "evolutionary" nature of the BTP's thinking, the outputs of any work undertaken by PwC would necessarily be at a high level.

Against this background, the terms of reference agreed with PwC asked them consider, to the extent they were able:

- Whether the plans (if any) produced by the BTP team to handover matters to the Transformation Management Office were sensible (it should be noted that this aspect of the work was predicated on the assumption that there would be a handover from the BTP team to the another, distinct team responsible for implementation, with no continuity of personnel);
- Whether the proposed high level implementation plan was well structured, identified interdependencies, took account of appropriate timing, balances the need to accelerate benefit release within funding, business capacity and capability constraints;
- Whether the benefits, operating costs and funding requirements seemed prudent;
- Whether (what was then referred to as) Plan B was credible;
- Whether the proposed governance structures were robust and suitable;
- Whether the assumptions underpinning the so-called "TOM" were realistic; and
- Whether the TOM, if implemented as stated, would deliver the required cost saving of £300 million by 2020.

The accompanying review paper presents PwC's response to the above questions, though it should be noted that not all matters above have been fully addressed. There were several reasons for this, with the obvious one being that (perhaps somewhat inevitably given the complexity of the subject matter and people's busy schedules), there were delays in accessing the documentation and data, with final versions of certain documents being produced relatively late in the day. In consequence, PwC were given a somewhat compressed timetable to undertake their review, being only able to look at the materials as they have become available. That said, both the McKinsey and the PwC teams have worked closely since the documentation settled down and, as you may see from David Ryan's paper, where time has allowed, a number of suggestions made by PwC in order to "de-risk" matters have been taken into account by the BTP team; some of these are now reflected as items to be addressed during the so-called "transition phase".

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3. Brief comment of the structure of the report, the risks and macro themes

The PwC report is designed to be self-explanatory and tries to strike a balance between commenting on the risk and other implications of the narrow core request set out in David Ryan's paper (which is "to progress the transition activities"), on the one hand, and the wider strategic initiatives (being the 6 themes and 13 distinct programmes), on the other. The reason for this approach is that, as commercial matter, it would clearly not be sensible to undertake a review of the proposal to undertake transition activities on its own (which in any event is a relatively straightforward exercise) if it were felt that the wider strategic initiatives were in some way irrevocably flawed (which is not their conclusion).

On reading all the papers, it will be seen that there is (by implication or otherwise) a degree of consensus in relation to the following propositions:

- That there are significant risks and/or adverse financial consequences associated with whatever road POL choses to take (including for this purpose, the "do nothing" option).
- That agreeing to the narrow core request is in itself not something which would be considered particularly risky.
- That any decision to start to implement, or to continue to implement (as the case may be), the 13 programmes carries with it either significant or very significant risks - these are referred to, and discussed, in both papers.

PwC do, however, go somewhat further and, helpfully in my view, frame a series of questions (in section 3) that the Board may care to consider during its consideration of this matter. Furthermore, there is a macro theme that surfaces in a number of places in their paper to the effect that the transition phase will need to focus on developing a clearer vision showing how all the various elements of the programme come together as a cohesive whole, rather than a series of separate initiatives. By contrast, and somewhat reassuringly, no red flags, which might cause the Board automatically to reject the work done to date, are raised.

4. Recommendations

The Board is asked to note the accompanying review paper from PwC on the Business Transformation Programme.

Chris Aujard
20 November 2014

POL00149638

Work in progress draft

Review of Business Transformation Programme

High-Level Themes

Board Discussion Paper

20th November 2014

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1. Executive Summary

This review is based on our view of the Business Transformation programme from documentation we have seen up to the 17th November. We acknowledge that the work is continuing to develop and to be refined and therefore different elements of the programme are evolving in real time. We believe however that our main conclusions and areas of focus remain relevant throughout the Board approval process for the next phase of detailed design of the transformation programme.

It is evident that significant effort and analysis has been undertaken by POL and its business partners to understand POL's current state and its need to achieve commercial sustainability by 2020. The current state has been validated with several site visits and c.190 processes have been thoroughly documented. This has provided a detailed understanding of how the business currently operates and some very useful insights have been drawn. Detailed revenue, cost projections and assumptions have also been made which build a forecast for the future state of Post Office 2020.

POL understands that it faces a declining revenue profile and a high cost base which is not sustainable going forward. In this type of turnaround situation, all routes forward will inevitably contain significant risks.

In reviewing the available transformation programme documentation we have sought to put ourselves in the shoes of a POL Board member. Four key themes have emerged that we highlight below. We have been advised that some of these will be addressed in the next phase of the programme – the Detailed Design Phase.

Themes:

1. **A single unified business case and integrated transformation programme still need to be fully defined and developed. This requires a compelling narrative to set out the case for change and the organisation's response.**

   Our understanding is that the transformation journey for POL will combine the Commercial Strategy, the FS Strategy, the 13 programmes that comprise what is termed the 'Business Transformation Programme' and the 3 levers (Plan B options) designed to respond to risks and challenges as they arise. To articulate the full programme of change, these individual programmes, initiatives and interventions need to be brought together into a clear Target Operating Model with a supporting Outline and a Detailed Business case incorporating detailed financial modelling, a benefits plan and approach, and risk mitigation actions.

   In this review we have focused on the proposed 13 business transformation initiatives which are focused on achieving a cost reduction target of £300m (the Business Transformation Programme). The commitment to this programme is strong as evidenced by ownership of different work-streams across a number of Exco members.

   We have not reviewed the financial modelling that underpins this programme and therefore cannot make any comment as to the validity of the assumptions used to calculate the potential savings, nor whether they are achievable.

   We have put together a high-level summary 'picture' of the impact on POL as a whole of the 13 programmes, so that it is easier to understand what the implications are for POL in 2020. We have also identified where we believe there are interdependencies between the 13 programmes and what the potential impacts are on POL's business model. We recommend that the next phase of detailed design develops this further to ensure that any unintended consequences of change are understood and avoided.

   The documentation we have reviewed has mainly focused on the cost reduction programmes. There are a number of revenue generating initiatives and programmes in the two business strategies, as well as in the 3 levers identified to adjust these'; the next phase of work should seek to bring these together more clearly into a fully balanced programme.

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2. **The environment and market conditions for POL are changing faster than anticipated. Further work is needed to identify all potential options around the three levers (previously Plan B) and more cross-functional working across POL to evaluate all options in light of possible impacts on other revenue streams (e.g. changes to supply chain and potential impacts for financial services).**

   The '3 levers' work provides good analysis of the challenges and options facing POL around revenue growth. However, it does not yet reach a final recommendation. Continued assessment is required to identify the cost / benefits of these ideas and potentially to further develop new revenue opportunities. Clarity is needed on how they impact the business model and high level target operating model, for example:

   - POL needs to make key decisions around its channel mix and future portfolio (e.g. SME and E-commerce proposition). Before embarking on radical cost cutting the impact of cost reduction on the Post Office's ability to generate revenue in the future must be understood.
   - POL's relationship with Royal Mail is one of its greatest assets but also potentially a significant constraint to growth. As already identified, redefining this relationship as one of the key mitigation options responding to changes in the mails market; this therefore requires careful consideration before proceeding. More clarity is needed on the detailed options for change which are thought to be still within the boundaries of the MDA.
   - PwC has not seen the FS strategy documentation which went to the Board previously and therefore cannot comment on this component of the business model. However, we can provide a point of view on the future of the retail and commercial banking landscape in the UK over the next 3-5 years and the potential impact this might have on POL.

3. **The Transformation Blueprint is a high level plan which defines some of the next steps for transition of the cost reduction initiatives from Design into Delivery. There are a number of key activities that need to be completed as the programme moves into detailed design before it can transition into delivery. A distinction should be made between those initiatives already underway and new programmes.**

   The 13 initiatives within the Business Transformation Programme should be brought together into a single integrated portfolio and with a consolidated plan so that there is full visibility of their interrelationships and any interdependencies.

   We have identified a number of activities / documents that should be developed in the next, Detailed Design Phase of work. This includes items such as a detailed resourcing plan, an impact assessment and the benefits management mechanism.

   For example: POL already recognises that the organisation does not currently have sufficient capacity or capabilities in-house to deliver such an ambitious programme of this complexity and magnitude. At a high level, indicative team sizes have been identified for each of the 13 programmes. A consolidated resource plan is required to provide clarity of the skills and capabilities required to deliver the transformation, and a resource profile is needed to show the volume and timing of resources required across the lifetime of the programme. This is important to enable informed decisions about recruiting, training from within or 'buying in' temporary support. In such a large transformation, POL must fully understand the cost implications of different resourcing options, and the timing of the resource needs in order to avoid delays or damage to benefits realisation.

   Clear and effective governance is required to drive the portfolio forward at pace. This should include the creation of a Design Authority to hold individual programmes to account and to preserve the Post Office 2020 vision.

   A portfolio of this complexity which impacts staff, customers and other key external stakeholders requires a robust change management strategy; this should include communications, stakeholder management, training and development for staff and other targeted interventions to align POL senior leadership behind the change. A robust strategy for union engagement will also be important to avoiding IR action if possible.

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4. **The transformation programme by its very nature has a high risk profile. Some of the risks have satisfactory risk mitigation strategies identified, but there are some gaps. Therefore the next phase of work should seek to address this and put in place adequate steps to address these risks.**

   POL should not underestimate the cumulative impact of significant and multiple risks to delivering BAU services when embarking on such large scale transformational changes concurrently. In considering these we acknowledge that there is also potential adverse financial risk associated with the 'do nothing' option due to declining volumes in the mails market and some government services, as well as competition in financial services and telecoms.

   Robust risk management on a portfolio of this magnitude is essential. Further work is needed to model risks while detailed mitigation plans need to be developed to provide assurance to the Board that the portfolio is realistic and deliverable.

   The proposed 13 transformation initiatives aim to achieve cost reduction of £300m, with a £1.1bn of Government funding requirement. However the delivery risk associated with many of the initiatives is high and the barriers to overcome are challenging. The programme will be sensitive to its low ROI (21%), however it should be noted that this figure is supressed due to the low ROI on the network transformation programme which is already underway and agreed with Government.

   The main imperative is to take cost out to stabilise the Post Office while looking to grow revenue elsewhere in a competitive market environment. We have not seen documentation that fully addresses the irreversible impact that cost reduction will have on its ability to change tack or explore alternative sources of revenue in the future.

   A number of the 13 initiatives have interdependencies with each other and also existing BAU initiatives which are outlined at a very high level. A much clearer and more detailed understanding is required for the next phase.

   The Business Transformation Programme has evolved at tremendous pace and it is important that all of the organisation's leadership have the same level of understanding and commitment to the proposed changes.

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2. Background

Facing significant financial and competitive pressures in a rapidly changing market, and a new paradigm of being a separate entity from Royal Mail, Post Office Ltd (POL) has identified its stated objective of becoming commercially sustainable by 2020. This vision is supported by a strategy which comprises two core customer propositions:

1. The most convenient mails & parcels retailer
2. The UK's leading challenger in Financial Services

In May 2014, POL embarked on a Business Transformation Programme (BTP) to deliver this vision underpinned by a streamlined and cost effective operating model. This programme identified a £300m gap for POL that would need to be addressed. In recent months a radical cost reduction programme has been designed which contains 13 transformation initiatives which will deliver the £300m saving and leverage £1.1bn of previously agreed Government funding. This cost reduction programme represents the 'TOM' that we have been asked to review.

In parallel, a separate project has identified 3 levers to adjust the strategy to respond to challenges and risks as they arise (Plan B options) which threaten to undermine the strategic direction that has already been agreed.

Finally, there has also been work carried out to address the People and Organisational design of POL recognising the current capability and capacity of the existing organisation versus the requirement for top talent to lead and drive the immense amount of change required by the organisation over the next 5 years.

The Board will meet on 26th November 2014 where they will be presented with the Business Transformation Programme and they will be asked to:

- Provide board alignment, assurance and support for the proposed way forward at the completion of Business Transformation stage I and II

Approve next steps for transition to put in place the critical success factors for transformation implementation. We recommend that the Board give careful consideration to the 4 themes outlined in the Executive summary and the detailed findings contained in the remainder of this report.

2.1. The Post Office in 2020 – what will be the impact of the Business Transformation Programme?

One of the key themes in the detailed section of this report is the requirement to have a visual representation of how the Post Office will change from the current state through to 2020. As part of the Transformation roadmap, 13 initiatives have been identified to shape the future of Post Office and enable it to become commercially sustainable by 2020. A number of these initiatives are already in progress (e.g. Network Transformation, Crown Transformation etc.) whereas some of them will kick off before the end of 2014/15 (e.g. Finance/ HR Transformation). The diagram below is a snapshot of POL's current state and target state that has been developed to understand the scale and scope of the changes the organisation will go through. We have attempted to 'paint a picture' what we believe POL will 'look like' in 2020 if the full set of transformation initiatives are implemented to assist the Board in visualising the impact of the transformation.

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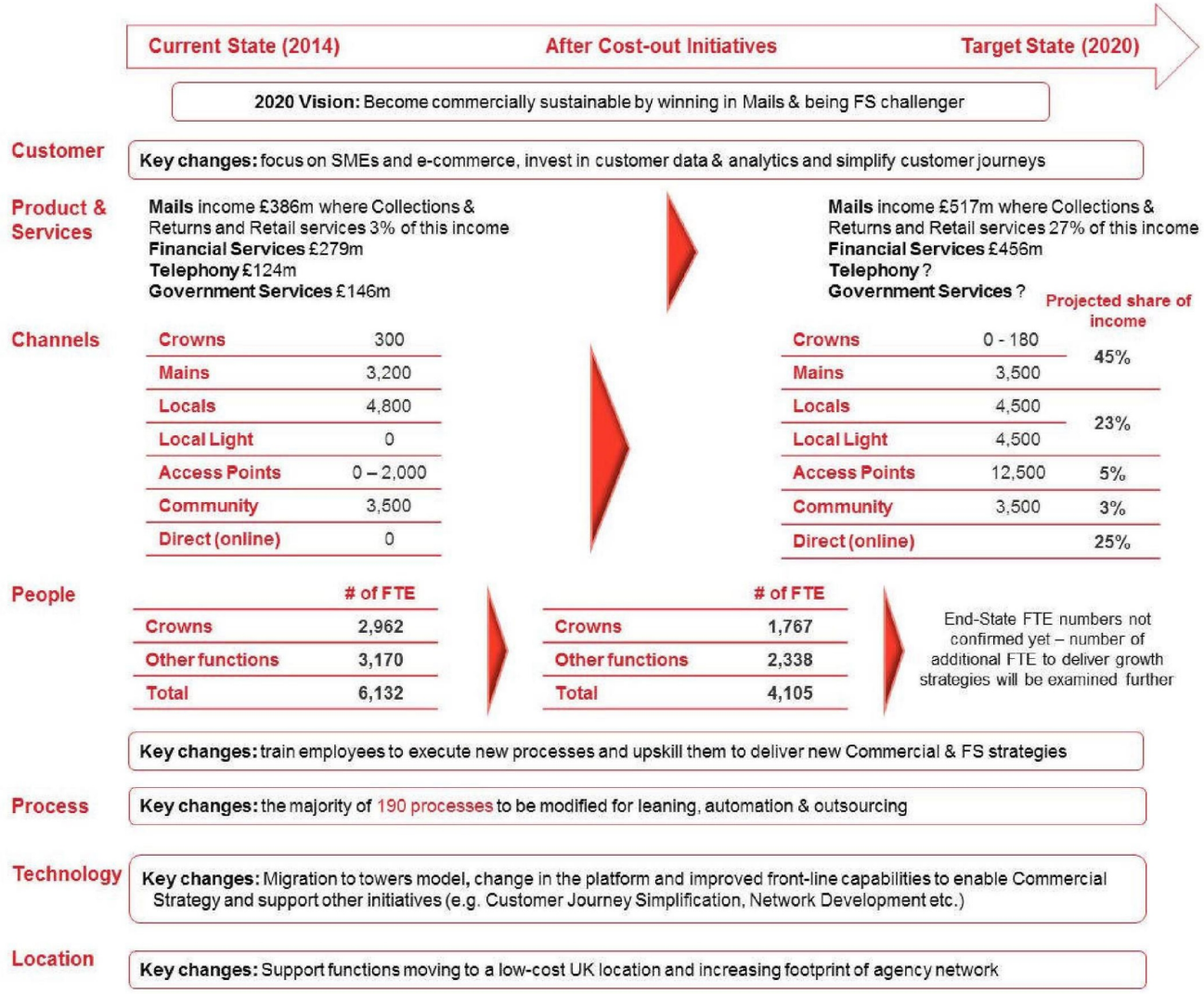


Figure 1: Summary of main changes identified in Business Transformation Programme

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3. Review of the Business Transformation Programme

We have reviewed the material that has been provided on the Business Transformation Programme. We recognise that the programme has continued to be developed and to evolve and therefore we have reviewed the material that we have been provided with up to the 17th November. We also acknowledge that some of the findings that we have identified over the past two weeks have already helped to shape the programme and that some of the issues were promptly addressed.

There are a number of documents that have not been reviewed as these have not been available, such as the economic model that sits behind the cost saving projections; therefore we have not tested the modelling or the assumptions that underpin the programme.

The documentation that we have reviewed has often been brought to life through the 'voice-over' when presented, for example by the Exco members to their colleagues. To aid clarity for this review we have summarised in Appendix 3 our understanding of the 13 transformation initiatives.

In the table below we outline a number of themes that summarise our findings from the review of Business Transformation Programme. We have included some questions that we might ask if we were in the Board's shoes to provide comfort as to whether the transformation programme is fit-for-purpose, is deliverable and will not inadvertently damage POL's future ability to grow revenue / move in a different strategic direction.

Theme	Board Questions	Findings
Seeing the big picture The level of change proposed for POL is significant. Different strategies, initiatives and programmes all suggest a radically different Post Office for its staff, agents and customers. Visualising what this looks like would bring the impact of these changes to life and aid decision making.	*What do the changes mean for the shape of the Post Office?* *What impact will changes have on people, process, technology and customer?*	We have not seen a visual depiction of the Operating Model (As-Is and End State) that would help the Board and other stakeholders understand the vision and impact of changes on the organisation. A traditional Target Operating Model is the conceptual view of how the Post Office will operate in the future and how its resources work together and are deployed to achieve its strategy and serve its customers.
Fit with strategy Following the ExCo meeting on 13/11 we gained a better understanding of how the Post Office Commercial and FS Strategies, the Cost-Out programme and 'Plan B' options together form the full transformation programme. As these Strategies and programmes are somewhat separate initiatives, POL must be sure that in combination the actions that will be taken in the transformation programme will deliver the Strategic Vision for POL in 2020	*Does the programme allow us to execute our overall strategy?* *What do the changes required for cost reduction prevent us from doing in the future?* *What compromises between strategy and cost reduction have been made?*	The overall picture of how all the elements (Commercial & FS strategies, Business Transformation Programme – both on-going initiatives and new programmes, 'Plan B' etc) fits together and becomes a coherent modernisation programme is not clear. There are other elements that we expect to see that are not mentioned such as a property strategy. Without clarity of the programme, and simple 'story' of how everything fits together, delivery of this programme will be difficult, and there is a potential risk that it will not provide a compelling case for Government who are expecting a full 'network modernisation programme' with a balance of revenue, cost, people and operating model changes.

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Theme	Board Questions	Findings
Designing the full transformation / modernisation programme We have seen a number of elements of revenue generating ideas and cost-out initiatives, but as part of a full transformation programme further detail is needed in order to really test the validity of costs and benefits, risks and issues and implications for the organisation, franchisees, the public and government.	*What is the detailed cost and benefit profile from all the difference programmes / initiatives that would make up the transformation (modernisation) programme?*	At present there isn't a formal business case for the transformation programme. An outline (and then detailed) business case based on a holistic understanding of all elements of the Transformation Programme is required. This would clearly articulate • What the programme is • What the assumptions are • What the cost of implementation is • What the expected benefits are the profile of when the benefits are expected to be realised We would expect a business case to identify ranges of costs and benefits rather based on different assumptions.
Sustainability of the Change The Cost-Out Programme has been created to meet the Post Office's vision of becoming commercially sustainable by 2020. However, in isolation from in-flight initiatives, and without a holistic approach that flows from the new business model that understands the resources needed to deliver this, this may not be sustainable in the long term, or sensible to achieve the overall strategic objectives.	*Do the cost reduction initiatives impact current or future revenue opportunities?* *What processes and behaviour is changing to ensure changes are sustainable?*	To implement change in such a way that it is sustainable requires different methods and techniques. Consideration needs to be made as to how to implement as it is as much about behaviour change as it is about new methods or 'forcing' ways of working through automation. We would require more details on both the impacts on people, and the approach to be taken to change implementation in order to be reassured about the sustainability of the change proposed in the programme.
Focus on Strengths The design of a transformation programme should take a balanced view of strengths and weaknesses of the current operating model and organisational assets (in the fullest sense) as well as consideration of the market environment and forecast trends.	*Have all revenue opportunities and cost reduction options been identified and fully evaluated?*	In the material we have reviewed we have not seen a sufficient exploration of the strengths of Post Office. E.g. Recent work by Strategy&[1] identified that many traditional physical retailers are underplaying their positional advantage. We see many organisations rushing to move to a digital offering at the possible expense of making the best of the unique advantages they already possess. To succeed in digital also requires significant physical infrastructure.
Financial assumptions A financial model and assumptions sit behind the figures shown in the power point presentations.	*What are the core assumptions and cost drivers for savings?* *What activity or behaviour will actually change to enable cost saving of staff if network is increasing?*	We have not had sight of the financial modelling and are therefore unable to comment on the veracity of the assumptions contained within it. We have seen some inconsistencies in the numbers in the different versions of the documentation that we have reviewed – figures have been updated in different iterations but without an explanation as to the evidence for the change.

[1] Previously Booz & Company

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Theme	Board Questions	Findings
Understanding the journey The narrative for changes underway and planned at the Post Office has been largely verbal in meetings and board sessions. The story of change should be widely and simply understood by stakeholders.	*What is the narrative of transformation?* *How do conclusions flow logically into the decisions that are needed?*	Misunderstandings and the difficulty to carry out our work has largely been due to the lack of a single, digestible story of transformation. To do this kind of transformation really requires a powerful articulation of WHY things need to change and what it is that is actually changing. This provides the basis for all communications and engagement with staff, agents, partners, government, stakeholders etc. To provide comfort that the programme will achieve the strategic vision for POL will require a better articulation of the programme – what it is and how it will deliver the desired outcomes.
Return on investment The benefits case for transformation, whether financial, social or to achieve core elements of commercial sustainability needs to be understood and explained. This is particularly true where ROI is low and wider stakeholder funding may be required. The 13 initiatives provide a total benefit of £282m, but require £1.1bn funding to deliver ROI of only around 13%[2].	*Why is ROI low and is it reasonable?* *What confidence do we have in revenue growth and cost assumptions?* *What are the benefit dependencies?*	A business case for each of the 13 initiatives is needed to understand how ROI is calculated and aligned between programmes to justify the level of investment required. Without exploring the supporting models to test market assumptions and forecasts, we believe there is significant risk that these will further contract and affect returns.
Transformation knowledge and capability Our greatest insight has come from our limited opportunity to speak to those involved in the programme. But, this pool of individuals is small and the number of permanent employees with a programme perspective is minimal.	*Who can provide continuity and comfort that knowledge is sufficiently shared?* *How are we sharing knowledge in the programme?*	With the lack of single documented narrative of transformation, much of the story of transformation is 'in the head' of key individuals in the programme who are temporary or external to POL. This is a significant risk and knowledge needs to be shared and transferred across POL.
Risk Profile Many of the initiatives carry a high degree of risk – both delivery risk for example the reliance on being able to change the nature of agreements with core partners or the need for Government support, and risk for the organisation e.g. reputational risk. All risks should have adequate mitigating actions identified and planned.	*What is the worst case scenario?* *What is our mitigation in worst case scenario?* *Does this represent too much risk for POL?*	The programme has an acknowledged high risk profile and 3 main levers will be used to respond to risks as they arise. Market conditions have already moved significantly in the last 6 months, and the ExCo already agreed on 13/11 that some of the original 'Plan B' measures should be incorporated into the main approach. This recognises the mitigation required in order to keep up with the sector and competitive landscape change. However, considering the programme's significant delivery risk, we have not yet seen sufficient evidence of risk mitigation and scenario testing.
People Impacts It is recognised that there is insufficient talent and capability within the organisation for the level of change required. We have not had sight of the People and organisation design and understand this has been conducted as a separate programme of work. It is critical that the output of this work is considered in conjunction with Business Transformation	*How are we communicating changes and staff impact?* *Are we managing to retain and attract talent?* *Has TUPE been factored in for migration from crowns to local*	Although this has been flagged by the Transformation team, PwC have not had visibility of the detail of analysis or planning that has taken place. Upskilling the organisation and attracting and recruiting new talent to source new skills required to deliver the strategy e.g. FS skills will be crucial. Knowledge retention (e.g. the centralisation of sorting at PostNL failed due to the loss of local knowledge that was not properly captured before the organisation

[2] The previous iteration identified 21% RoI

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programme and the levers which may be applied as risks arise. A lot of operational change is proposed as processes are automated or outsourced. A strength of the Post Office is the level of local knowledge that makes sure the business functions well on a daily basis.	*agencies?* *Will knowledge and capability be lost if we reduce the number of crowns and move to automated / outsourced processes*	moved to a new operating model) should also be a core consideration during transition.

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4. Three Levers to adjust Post Office strategy (Plan B options)

'Plan B' was introduced to respond to the situation where the market conditions / competitive landscape worsened and the assumptions underpinning the Strategy are no longer valid. This has now been developed into the identification of three 'levers' which will impact on the future of POL.

These three levers (Plan B options) provide some positive risk mitigation. The next step is to agree these options and embed them into the overall transformation programme so that they are included in the business case and target operating model. At the current time, the three levers have not been worked through to the point at which concrete conclusions have been made and recommendations are ready to be discussed and agreed.

Note: The documentation under review here continues to change.

Plan B lever	Board Questions	Findings
1) Working with other partners		
IRRELEVANT IRRELEVANT Plan A+) **IRRELEVANT**	*What are the core barriers to resolve IRRELEVANT and POL corporate and strategic misalignment?* *How can we validate the respective strengths of POL and IRRELEVANT in IRRELEVANT negotiation?* *What is the risk of disintermediation and who offers the greatest threat as an alternative retail access point?* *If some form of Plan A+ activity is needed in the medium term, why isn't this in Plan A?*	This lever considers **IRRELEVANT** **IRRELEVANT** **IRRELEVANT** (Plan A+). However, financial analysis of this scenario suggests there might be some significant impacts on volumes going through the Post office network. Robust evaluation and modelling is required before a strategy can be decided upon, as the repercussions of a wrong decision with regard to the IRRELEVANT relationship could be very damaging and irreparable. Despite some stated benefits of greater universality, in the medium term with shifts in strategic direction elsewhere and the known quality of service and reputation of IRRELEVANT the trigger for this lever should be high. As customer journey options increase, there is a significant, irreversible risk of disintermediation and we would like to see more consideration of how this risk would be addressed in this scenario. **IRRELEVANT**
2) Further cost out and channel shift		
If income continues to show low growth to undermine commercial sustainability, the POL may reconsider its approach to market. This can include stalling the roll out of new formats, reducing high cost channels (Crowns, Mains) and investing in digital.	*If we choose a particular solution for revising our channel mix, what would be the implications on our strategic objectives?* *Do any of these proposed solutions undermine the delivery of our core propositions?*	**Aligning to strategic direction** A comprehensive list of potential changes in the channel mix is identified but an impact assessment needs to be carried out to better understand the implications on POL strategic priorities. For example, we would expect to see the details of the 'agency-based sales structure' for FS products as opposed to Crown sales as an alternative solution suggests accelerating the Crown divestment. Similarly, the role of Mains in the FS revenue growth is not clear during agency migration.
	What triggers will initiate the adjustment of the proposed channel mix? *Which lever is the most appropriate one given a particular low growth*	**Adjusting the channel mix in a robust way** 3 broad levers for adjusting the channel mix to respond to low income growth are proposed but a mechanism to ensure that the right lever is used as needed depending on the downside scenario. There will also be an impact of these on the financial flight path which needs to be drawn out to give Board the confidence that this

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	scenario? *How will the suggested channel mix impact our financial projections?*	lever can robustly react to downside scenarios.
	What is the role of digital in increasing our revenue? *Can our IT investments flexibly deliver new digital services?*	**Increasing role of Digital** The growing role of Digital has now been recognised in the Plan A toolkit, not just Plan B. But, it supports two core propositions due to changing dynamics of consumer behaviour and its thinking needs to be embedded to ensure sufficient investment in the required IT capabilities and to accurately capture the IT architecture requirements and roadmap from a broader range of digital offerings.
	What are the resource implications of 'Plan B' options? Do we have the capability and capacity to deliver these options if our main plan cannot be realised? *How does this impact our cost base?*	**Alignment between Cost-Out Initiatives & 'Plan B' solutions** The impact of cost-out initiatives in Plan A should be taken into account while deciding on the proposed actions in Plan B. The resource and cost implications of these levers have not been clearly articulated. With a smaller proposed TOM, these solutions will put extra burden on the downsized functions. For instance, making Mains viable in a low income growth scenario expands the work of reduced Network Support Teams following Network Support Transformation.
3) Strategic Portfolio Management		
This sets out an ongoing process to evaluate, adjust and re-prioritise elements of the product portfolio to continually appraise products and services according to performance and resource constraints. If POL's core market does not deliver growth, new markets and service options will be considered.	*Can our new Target Operating Model allow for the new products/ service offerings to be added to our operations quickly?* *Will these new offering require a different set of internal capabilities?* *Should this not be included in Plan A?*	**Agile Operating Model for new income streams** The proposed portfolio management discipline provides a robust and systematic way of evaluating new product/ service offerings, however the implications of these new income streams on the TOM should be considered in more detail. It is critical to develop an agile operating model that will allow new product lines to be delivered efficiently and effectively in a short time period.

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5. Review of Transformation Blueprint

At PwC we use a framework to design large scale transformation programmes. This framework is called 'Transform'.

Transform has been developed over a number of years based on our experience implementing large-scale transformational change across a range of organisations and sectors. Through our knowledge of what works, and what doesn't, we have developed this best practice framework which include all the activities and elements that need to be in such a programme to successfully deliver change and achieve the expected benefits.

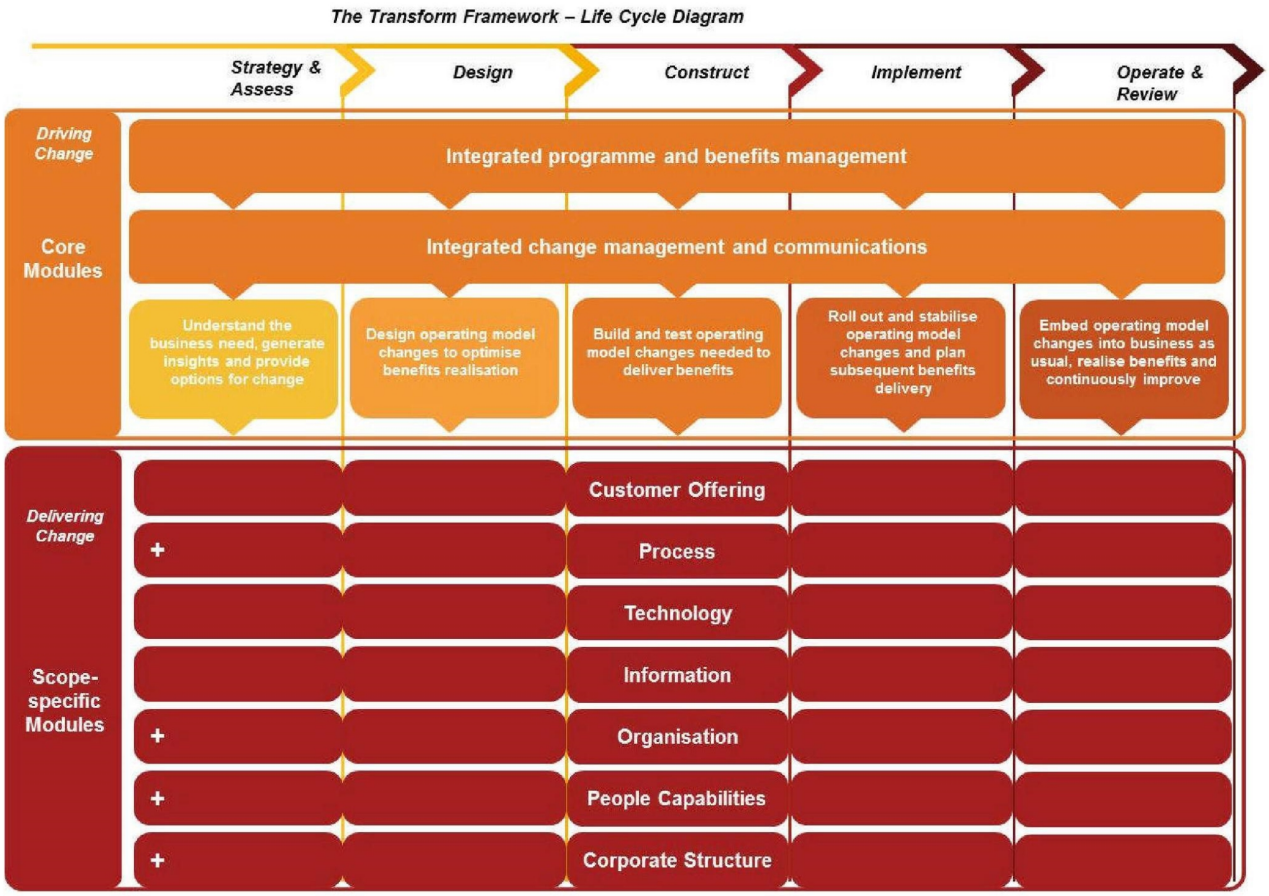


Figure 2: PwC's Transform Framework

POL is currently in the *Design* stage of the five stages shown above. As the programme moves into a "Transition to Execution" stage, the following areas should be addressed to enable a successful implementation of the 13 initiatives through the *Construct*, *Implement*, and *Operate* phases.

Key Areas	Potential Consequences of not addressing
1: Detailed Resourcing Plan An estimated team size for each of the thirteen programmes has been indicated, but this has been difficult to test given the lack of detailed rationale to explain the team size. Given the size and scale of the POL transformation programme, a detailed resourcing plan should be developed in Transition Stage to ensure that the required capabilities and skill-sets are in place as well as sufficient capacity for detailed design, build, and implementation of the transformation programme.	The lack of a detailed resource plan will put undue strain on POL; scarce skills will not be optimised; and subject-matter experts will face competing demands from different projects. In addition, targeting gaps in skill and capability will be difficult to achieve making the development of a compelling business case to secure additional internal and external resources more challenging.

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Key Areas	Potential Consequences of not addressing
2: Impact Assessment We have not seen assessments of the impact of each initiative on a range of aspects; including people, technology, business outcomes, customer service, brand and reputation. The implications of the initiatives on each Operating Model layer (i.e. process, people, technology etc.) should be outlined to inform the detailed design of TOM.	Without impact assessments of each programme and any suggested changes to programmes, the Board will be left making uninformed decisions that may have unintended consequences on aspects of the organisation or its ability to serve the customer.
3: Role Definitions The delivery partner roles require more detail and explanation as they are critical to the next phase of the programme. The rationale behind the separation between design partners and implementation and outsourcing partners is not fully understood.	Roles not clearly defined will lead to confusion, key activities may fall between the cracks, and there will be a blurring of accountability leading to an inability to hold individuals and teams to account. Too many delivery roles, potentially supported by a number of different delivery partners will also increase the management burden and lead to unnecessary confusion.
4: TMO Design, Structure, and Set-Up The role of the TMO is critical for the success of this transformation. The main principles considered to set up a TMO seem to be appropriate, but the size and shape of this function and the roles involved should be defined further. For instance, two to four liaison roles in the team may not be sufficient given the demands from thirteen initiatives and the role of Head of Business Analysis and Design needs to be better articulated.	Getting the shape, size, and functionality of the TMO correct from the outset is critical to secure the correct skills and expertise to form the team. A TMO that cannot add value to programme teams but merely appear to be an additional reporting burden will quickly be side-lined by the business.
5: Risk Management Processes and Structures Given a transformation of this size, it is critical to apply a rigorous risk management discipline. We have not seen evidence of this being in place. For example, risks do not appear to have been modelled, so it is difficult to validate the RAG status. No risk owners have been assigned, nor does there appear to be the governance in place to support risk elevation in the organisation. We would like to understand risk mitigation actions better. It is important to develop detailed mitigation strategies in particular around trade union actions and Government position and appetite.	Without a tight grip on risks and a robust risk-management discipline, a transformation programme of this scale will quickly become unmanageable. The Board will have to take tough decisions and they need to be able do so from an informed position with a clear understanding of key risks and associated mitigation plans otherwise risks such as Trade Union and Government negotiations are likely to become key barriers to a successful outcome.
6: Benefit Management Mechanism High-level financial benefits are identified to a varying extent for the thirteen programmes. We have not had sight of the detailed financial model behind the initiatives. Non-financial benefits such as reputation and customer relations do not seem to have been considered. Benefits Management is a key area that needs to be planned and resourced properly from the outset. We often find that in transformation programmes of this type, this is not addressed and as a result benefits are simply not realised.	Without a full appreciation and visibility of the forecast of both financial and non-financial benefits, it will be impossible for the Board to know whether the programme is on course to deliver what is setting out to do nor will they be able to hold programme leads accountable for any failure to deliver anticipated benefits.
7: Governance and Reporting The proposed governance structure seems sensible, but further work is required to lay out the details of the governance mechanism, such as escalation routes and frequency of meetings.	Successful programmes have clear, robust, and well-understood governance. Without this there is a risk of programme proliferation and decisions being made in silos with little control over the impact these decisions will have on other parts of the portfolio. Equally, overly complex governance will stymie decision making and delay programmes unnecessarily.

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Key Areas	Potential Consequences of not addressing
8: Communications Plan As the programme moves into the 'Transition to Execution' stage, a detailed communications plan should be in place to appropriately engage with key stakeholders, including customers, employees, Government, Union, agents, and partners such as Royal Mail and Bank of Ireland.	Without an agreed narrative and robust communications strategy, rumour control will take over, and stakeholders will be unable to connect with the change and understand how it will impact them. In the worst case, this will lead to organisational paralysis, significant staff and trade union dissatisfaction, and adversely-affected customers.
9: Change Management Approach It is essential to have a clear understanding of the scale and scope of the changes proposed. The impact that this transformation will have on the organisation is huge and there should be an appreciation of the challenges that lie ahead, in particular the significant cultural shift from a public-sector mind-set to a private-sector, profit-making one, as well as a recognition of the leadership alignment issues both at Ex Co and in particular within the SLT.	Unless the change management is embedded in the integrated programme management, the transformation will not deliver the required cultural shift properly within the organisation leading to a loss of benefits. Staff will become disaffected, translating into a reduction in customer service standards. Without significant training and development for the organisation on what and how they will need to do in the future many of the benefits will not materialise.
10: Portfolio Plan As the programme moves into Detailed Design stage, we would expect to see a high-level portfolio plan outlining the key activities and the dependencies between the thirteen programmes and other change initiatives. This should also include high-level assessment of business as usual activities to ensure resource hot-spots are managed properly.	Without integrated planning, people will struggle to differentiate between business as usual and change, not be able to understand the organisational priorities, programme alignment will be lost, and ultimately the transformation will fail to deliver all intended outcomes.
11: Detailed Handover Plan It is a good starting point to develop high-level next steps as part of the Blueprint, but we would expect a detailed handover plan to be in place to gain confidence over whether it could be implemented against the financial backdrop before the Board are in a position to make the go/no-go decision.	Confidence in the transformation journey is crucial for minimising risk and increasing the chance for success. Prioritisation, sequencing, alignment, and similar decisions need to be consciously made at the outset; not once it is potentially too late.

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6. High Level Risk and Mitigation Action Review

To pursue the 13 initiatives set out in the Business Transformation programme we have identified 4 categories of risk that need to be considered. Alongside a summary of each risk, we also indicate whether we have seen evidence that this risk is being mitigated from the documents in our review. Although there is some good analysis to identify risks, this often does not always follow into mitigating actions. As such, this does not provide comfort of a comprehensive view of the mitigation of risks, the interdependency of those risks and the impact that their mitigation will have on other initiatives.

It is critical to revisit key risk areas and develop detailed mitigation actions as part of the next stage.

	Initiatives	Delivery (programme, people)	Reputational	External Stakeholders (unions, Gov't, NFSP)	Financial	Key Dependencies
Reduce Central Costs	**1a** Near-term cost out	High volume of change & support (incl. delivery partners) required to deliver in business	Adverse impact of Union actions on the public goodwill & brand trust and disruption on BAU	Potential union disruption which may also trigger Government reaction	Further funding due to delivery issues and decrease in the capacity to deliver revenue growth	
	1b Finance/ HR Transformation					**3**
	1c Network Support Transf.					**3**
	Mitigation	PARTIAL	NONE	PARTIAL	NONE	
	1d Long-term efficiencies	Medium volume of change following from near-term cost-out initiatives	Adverse impact of Union actions on the public goodwill	Potential union disruption which may also trigger Government reaction	May not deliver savings. Decrease in ability to drive revenue growth	**1a, 1b, 1c, 3**
	Mitigation	NONE	NONE	PARTIAL	NONE	
Transform the Organisation	**2** OD & People Development	**Out of scope**				
Lean IT	**3** Lean IT	High volume and pace of IT change to enable other initiatives	Disrupt access to POL services	Failed IT delivery to trigger negative reaction	Budget unable to cope with demand and delivery partner issues.	
	Mitigation	IN PLACE	IN PLACE	NONE	NONE	

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	Initiatives	Delivery (programme, people)	Reputational	External Stakeholders (unions, Gov't, NFSP)	Financial	Key Dependencies
Reduce & variabilise network costs	**4a** Network Transformation	Team changing and dependent on evolving models	High market risk	Changing scope of programme	Replacement partners needed for agents	**1c, 5a, 4b**
	Mitigation	NONE	PARTIAL	PARTIAL	NONE	
	4b Crown Transformation 2	Agents required to migrate activity from Crowns	Brand impact from fewer Crowns in key areas	Likely union disruption	Transferring Crowns to Agents cost and loss of revenue	
	Mitigation	NONE	NONE	NONE	NONE	
	4c Customer Journey Simplification	Dependency on IT and with other programmes	Requires shift in customer behaviour	Royal Mail support, NFSP action	Cost efficiency improvement is not met	**3, 5a,5b**
	Mitigation	PARTIAL	NONE	PARTIAL	PARTIAL	
Win in Mails	**5a** Network Development	Large change with pressure on people capability to deliver	Sensitivity to market and footfall	Royal Mail support, NFBP action, retailer negotiation	Agent time can't be easily transferred to benefit	**3, 4c, 5b**
	Mitigation	PARTIAL	PARTIAL	NONE	PARTIAL	
	5b Commercial Strategy	Cost or vision not defined, g estimate, people capability	Market conditions drive lower income	Royal Mail relationship changed to allow competition	Income not underpinned by operational plans	**3, 4c, 5a**
	Mitigation	PARTIAL	PARTIAL	NONE	NONE	
Win in FS	**6** Financial Services Strategy (FS strategy not defined and less information available for review)	Needs substantial investment in people capability and training	Market competition, poor capability from staff and 3rd parties erode brand	Bank of Ireland support required beyond 2023	Competition with big banks, market saturation, reliance on POL brand/branch network	**3**
	Mitigation	NONE	PARTIAL	NONE	PARTIAL	

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Colour	Risks – Description
	High risk – high likelihood, high impact
	Medium risk – medium likelihood, medium impact
	Low risk – low likelihood, low impact
Text	**Mitigation – Description**
In place	Mitigation action in place that will reduce risk impact
Partial	Mitigation action proposed, but does not seem to sufficient to offset the impact
None	No evidence of mitigation action in place

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APPENDIX I – Documents Reviewed

Documents	Documents
20131120 Strategic Plan November BIS Submission FINAL	BTr end of Stage 1 summary
20140211 ExCo Paper 13 Feb 2014 v0_1TL Final	BTr Stage 3 Exco doc_v 02
20140226 Business Transformation_Board_Brief v0 4 Final	BTr Stage 3 Appendix 1 - Programme scopes and financials
20140320 Business Transformation_Board_Brief_11	BTr Stage 3 Appendix 2 - Risk assessment
20140320 Business Transformation Board Paper v21	BTr Stage 3 Appendix 3 - Delivery partners
20140410 BT Design Partner briefing v1.0	BTr Stage 3 Appendix 4 - TMO
20140508 Business Transformation_Exco_Brief_Final	Business Transformation Design Partner ITT
20140604 POL Board Strategy PREREAD	Business Transformation Org Chart
20140605 cover memo_formatted	Business Transformation PID
20140605 Steering Group and SME immersion final	Business Transformation Project Charter
20140702 Business Transformation_Board_Brief_TOM_Final	Current state assessments by business area
20140702 Operating Model and Strategic Cost Reduction	Exco working session 13th November v008 final
20140703 The 10 Accelerators	In-flight assessment validation deck
20141028 FINAL BTr Stage 2 Output_TOM Design v2	Lean walkthrough documents
20141028 Appendix 1 - Initial perspective on TOM attributes	Overall pain points
20141028 Appendix 2_Need to be true criteria	Process mapping output

APPENDIX II – Stakeholder Meetings

Name	Position	Date of the Meeting	Duration
David Ryan	Business Transformation Director	04/11/14	1 hour
Chris Aujard	General Counsel	05/11/14	2 hours
Alison Thompson	Head of Change	06/11/14	30 mins
Layla Wildon	Business Transformation (Corporate Services)	06/11/14	2 hours

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APPENDIX III – Our understanding of the 13 Business Transformation Programme Initiatives

Programme	Plain English Description	In-flight	Key outcome for POL	Potential consequence for future revenue growth	Commentary
1a Near-term cost out	Delivering cost efficiencies through leaning/ centralising/ stopping a number of processes and renegotiating supplier contracts	Yes	Reduction in central costs by £14m to be delivered by March 2017	It can enable further revenue growth by releasing capacity through efficient processes, however this capacity increase shouldn't be fully offset by redundancies	The programme requires major investment due to the volume of redundancies and TUPE transfers. Delivery of benefits in 2015/16 will be a significant challenge based on the volume of change that will be required (e.g. new processes, new ways of working etc.)
1b Finance/ HR Transformation	Delivering cost efficiencies through simple & automated processes, outsourcing transactional activities and centralising the retained function in a low-cost UK location	No	Reduction in Finance & HR costs by £6m to be delivered by March 2017	The FTE reduction may potentially decrease the capacity, undermining the ability to cope with the increased demand on back office functions due to revenue growth strategies (e.g. new income streams)	Proposed approach is aligned with current trends to make HR/Finance processes efficient and cost effective however, there are other operational performance improvement methods to release 20% capacity without any IT investment that could have been considered in this programme.
1c Network Support Transf.	Delivering cost efficiencies through simpler service catalogues, automated self-service network support, outsourcing transactional activities and centralising the retained function in a low-cost UK location	No	Reduction in Network Support costs by £8m to be delivered by March 2017	The FTE reduction may potentially decrease the capacity, undermining the ability to cope with the increased demand on network support functions due to Network Transformation & Network Development programmes	The Network Support requirements of each format (Crowns, Mains, Locals, Local Light and Access Points) should be mapped out and carefully assessed to mitigate any negative consequence of FTE reductions in the long-run.
1d Long-term efficiencies	Building on near-term cost out initiatives, delivering further cost efficiencies through operational efficiency improvements (e.g. lean/ automation)	No	Reduction in central costs by £17m to be delivered by 2020	Any further FTE reduction may adversely impact the capacity and capability to enable revenue growth	
2 OD & People Development	**Out of scope**				
3 IT Transformation	Transforming IT function to move to a lower cost model, migrate away from today's Horizon and improve front-line capabilities to deliver new functionalities (e.g. simple, online customer transactions)	Yes	Reduction in IT costs by £44m to be delivered by 2020 and key enabler for revenue growth as it delivers new functionalities	IT delivery is very critical for the successful delivery of revenue growth initiatives (e.g. Network Development, Commercial Strategy). Any slippage in the programme's timeline would impact the financial glidepath – especially the revenue growth projections.	The development of IT Architecture Roadmap is essential for the early identification of IT requirements from each initiative. IT terms of reference and findings need to be considered.
4a Network Transformation	The transformation of the Post Office's physical network to maintain size and capability	Yes	End state configuration based on a variable cost structure to meet profitability and revenue targets and moving to a new model of	Potential risk to growth in FS services due to reliance on Agency model to sell complex financial products. A wrong decision regarding match of format versus location may result in decrease of revenue and profitability.	To maintain the capability and footprint of POL, agents need to accept new models and adapt to new methods of service delivery which may impact service levels. No visibility of impact assessment although configuration now more conservative in its scope. Any change in formats and agents

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Programme	Plain English Description	In-flight	Key outcome for POL	Potential consequence for future revenue growth	Commentary
			3,500 mains, 4,500 locals, 4500 locals lights and 3,500 communities		remuneration schemes should be based on a micro market analysis to understand future revenue potential of micro markets as used by major European postal operators in their network transformation. In addition, the definition of formats should be expanded to have a better understanding of what products/ services will be provided by each format (i.e. Mains, Locals, Local Light)
4b Crown Transformation 2	Transition to a lower, variable cost base by migrating volume from Crowns to nearby agencies	No	Reduced number of Crowns (although this figure has been tempered in recent iterations)	Unable to leverage bricks and mortar for revenue generating opportunities with less control over agents and brand. It may also lower Post Office's credibility for potential business partners as generally agent based networks are less stable then own networks.	Crowns form a core component of the Post Office reputation and therefore form a PR risk. Majority of global postal operators Boards see own post offices as revenue drivers in prospering metropolitan areas, incubators for new services and products and simply part of their identity. These are lessened by the more muted programme of transformation now proposed but cost remains high as does the assumed migration of activity to agencies that will take place.
4c Customer Journey Simplification	Reducing customer activity and transaction time required for POL agent	No	Few steps in the process for mailing of letters and parcels are now to be carried out at the counter but through self-serve	As agent transaction times decrease there may be a deficit in capability in order to carry out tasks and field queries as required	We would like to see more evidence of piloting of changes to assess their impact on customer experience and cost. The simplification of the customer journey relies on a change in behaviour and a time saving which will not directly equate to a quantifiable financial benefit.
5a Network Development	Opening up to 12,500 access points with targeted retailers	Yes	Increasing the coverage of POL access points and introducing new offerings to offer an attractive proposition to host retailers	£64 additional income is expected (£51m Mails, £13m Bill Payment) based on an average income per access point of ~£5k. This assumes 4% annual mails market growth which may not be realised due to disruptions in the Mails market.	The locations of these additional access points should be economically justified based on the customer needs.
5b Commercial Strategy	This is the list of opportunities to grow profitable revenue in Mails	No	It is difficult to understand the impact on POL as references are made to key themes and these are not explained in any more detail e.g. SME, e-Commerce, Gov't, Home Services and Digital	An estimate of £30-50m has been made by 2019/20. However, this income is not yet underpinned by details of product offerings and operational plans	One would have expected more of the £1.1bn funding to be directed towards developing revenue growth. Within the levers for shifting the strategy (Plan B options) it would make sense to invest in these areas e.g. channels and products

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Programme	Plain English Description	In-flight	Key outcome for POL	Potential consequence for future revenue growth	Commentary
6 Financial Services Strategy	This is one of the 2 key pillars of the POL 2020 Strategy and vision and sets out POL's ambition to be a leading challenger bank by 2020	Yes	Diversifies products that POL can offer consumers through branches and networks to generate new revenue streams	FS Strategy is focused on leveraged POL brand and branch network to generate new revenue streams	PwC has had a lack of visibility of the FS strategy and the ExCo pack has limited details of the FS strategy compared to other initiatives. PwC has recently undertaken a Retail and Commercial Banking survey and have included a number of sound bites which we believe would be relevant to the POL FS strategy: <u>Positive indicators :</u> ">50% of consumers use branch network to open a mortgage, savings account or current account" "3 top drivers of choice for provider are: product attractiveness and price, convenience (branch location) and perception of stability and trust in brand" "UK retail deposit and mortgages set to grow to 2.7% and 7.8% respectively by 2017" "By 2017, Digital natives will be dominant consumer segment (>40%)" <u>Negative indicators:</u> "Despite media focus on challenger banks, market share from the survey suggests a low penetration"

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POST OFFICE LIMITED

Performance Report

October 2014

Produced By : Financial Control

For Queries & Comments Contact : Sarah Hall or Kam Bassra

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Headlines

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October 2014

Headlines

Operating profit before exceptional items in the month was £5.5m, £4.8m adverse to budget, bringing year to date operating profit to £29.0m and increasing the YTD shortfall versus budget to £23.4m (£36.0m adverse year on year, including NSP decrease of £23.9m).

Net income in P7 is adverse to budget by £6.7m and flat with last year. This reflects the continuing shortfall in Mails and Retail (mainly labels and delayed rollout of ebay returns) of £3.9m. Telecoms was £2.9m adverse due primarily to lower customer numbers and lower average revenue per customer. Government Services was £0.7m behind budget mainly due to fewer active POCA accounts than budgeted. To achieve the FYF of £880m, net income for the remainder of the year needs to average no more than £2.7m adverse to budget each month (and £3.4m better than prior year each month).

Net income year to date has worsened to £31.5m behind budget and £3.5m below this time last year (excluding NSP).

Total expenditure (before project costs) in the month was £0.7m favourable driven by the favourable subpostmaster costs relating to lower income, but offset by higher staff and non staff costs.

Total expenditure (before project costs) year to date remains favourable to budget by £10.2m.

The £60m savings task remains challenging with £7.7m still to be underpinned and a further £1.5m still in the 'hopper' to be validated (see page 7).

- Subpostmasters' Costs are favourable by £25.5m reflecting lower sales volumes and improved VAT recovery.
- Staff Costs are adverse by £2.5m reflecting under-delivery of savings tasks primarily in Supply Chain and Commercial.
- Non Staff Costs are £12.8m adverse driven by a £10m provision for client compensation, £4.5m shortfall in savings delivery, £3.0m for the Mails Segregation penalty payment accrual and other increased costs including postage. This is partially offset by increased VAT recovery of £11.0m.
- Project One Off Costs are adverse to budget by £2.4m reflecting unbudgeted spend for Sparrow and the 'Journey to 2020' strategy work.

CFO Forecast

The P7 CFO forecast remains the same as the half year forecast and projects net income of £880m (£45m below budget) and EBIT pre exceptionals of £85m (£14m below budget). This includes a profit contingency of £5m (see page 5 for further details). Work continues to identify and implement actions to recover the shortfall against target.

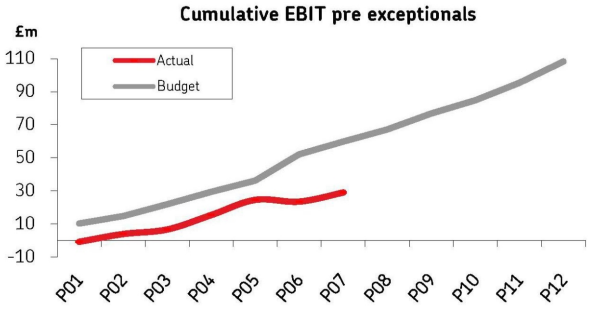
The task in the remaining 5 months is net income of £380m (compared to budget of £393m and prior year of £363m) and an EBITDAS loss of £8m (compared to budget loss of £18m and prior year loss of £38m).

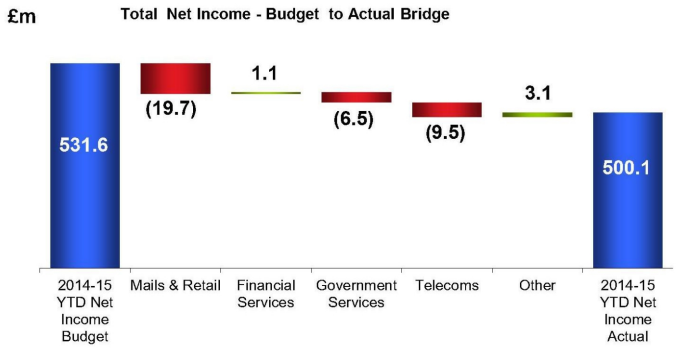
Crown Profit

The YTD Crown profit is £8.8m adverse driven by lower Mails income and higher property costs due to the delayed savings for the new Facilities Management contract as shown on page 6. The Q2 CFO Crown forecast is a loss of £13.8m which is £4.9m behind budget. This is aligned to the assumptions used in the business CFO forecast but excludes the contingency.

Network Transformation

The programme is ahead of plan at P7 both for contracts signed and branches transformed. The Mains model is performing well and the performance of the Locals model continues to improve steadily.





Financials	Year to Date Act	Target	Var
Total Net Income (excl NSP) £m (Bonus 20%)	500.1	531.6	(31.5)
Operating profit £m (Bonus 25%)	29.0	52.4	(23.4)
Crown Profit (Loss) £m (Bonus 12.5%)	(14.2)	(5.4)	(8.8)
Non Financials			
Queue time % < 5 minutes - Top 1k branches	77.8%	83.1%	(5.3)%
NT Branches Transformed In Year (Bonus 12.5%)	1,076	996	80

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Profit & Loss Statement

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October 2014

£m	Current Month Actual	Current Month Budget	Current Month Variance	Prior Year Period Actual	Prior Year Period Variance	Year to Date Actual	Year to Date Budget	Year to Date Variance	Prior Year YTD Actual	Prior Year YTD Variance	Full Year Q2 Forecast	Full Year Budget	Full Year Variance	Prior Year Outturn
TOTAL GROSS INCOME	**87.8**	**94.5**	**(6.7)**	**88.5**	**(0.7)**	**563.7**	**593.7**	**(30.1)**	**571.2**	**(7.5)**	**987.0**	**1,031.9**	**(44.9)**	**979.4**
Cost of Sales	(9.9)	(9.9)	(0.0)	(10.9)	1.0	(63.6)	(62.2)	(1.4)	(67.5)	4.0	(106.8)	(106.8)	0.0	(112.7)
TOTAL NET INCOME	**77.9**	**84.6**	**(6.7)**	**77.7**	**0.3**	**500.1**	**531.6**	**(31.5)**	**503.6**	**(3.5)**	**880.2**	**925.1**	**(44.9)**	**866.7**
Staff Costs	(21.7)	(20.8)	(0.8)	(22.2)	0.5	(146.0)	(143.4)	(2.5)	(152.6)	6.6	(233.6)	(238.7)	5.1	(253.9)
Subpostmaster Costs	(41.5)	(46.6)	5.1	(44.3)	2.8	(262.3)	(287.7)	25.5	(264.1)	1.8	(455.6)	(491.0)	35.4	(447.6)
Non-Staff Costs	(25.7)	(23.6)	(2.1)	(18.2)	(7.5)	(171.0)	(158.2)	(12.8)	(147.6)	(23.4)	(280.6)	(273.5)	(7.1)	(264.8)
Depreciation	(0.0)	(0.1)	0.0	(0.0)	(0.0)	(0.3)	(0.4)	0.1	(0.2)	(0.0)	(0.6)	(0.6)	0.0	(0.4)
Total Expenditure (pre POOC)	**(88.9)**	**(91.0)**	**2.2**	**(84.7)**	**(4.1)**	**(579.5)**	**(589.7)**	**10.2**	**(564.4)**	**(15.1)**	**(970.4)**	**(1,003.8)**	**33.4**	**(966.6)**
FRES - Share Of Operating Profits	2.8	2.7	0.1	2.6	0.2	26.6	26.2	0.4	25.3	1.3	35.0	35.0	0.0	33.1
EBIT - BAU	**(8.2)**	**(3.8)**	**(4.4)**	**(4.4)**	**(3.7)**	**(52.8)**	**(31.9)**	**(20.9)**	**(35.5)**	**(17.2)**	**(55.2)**	**(43.7)**	**(11.5)**	**(66.9)**
One off Project costs (POOC)	(1.6)	(1.3)	(0.4)	(2.9)	1.3	(13.5)	(11.1)	(2.4)	(18.7)	5.1	(19.7)	(17.3)	(2.4)	(26.0)
EBIT - Post Project Costs	**(9.8)**	**(5.0)**	**(4.8)**	**(7.3)**	**(2.5)**	**(66.3)**	**(43.0)**	**(23.3)**	**(54.2)**	**(12.1)**	**(74.9)**	**(61.0)**	**(13.9)**	**(92.9)**
Network Payment	15.3	15.4	(0.1)	19.2	(3.9)	95.3	95.4	(0.1)	119.2	(23.9)	160.0	160.0	0.0	200.0
EBIT pre exceptionals items	**5.5**	**10.4**	**(4.8)**	**11.9**	**(6.4)**	**29.0**	**52.4**	**(23.4)**	**65.0**	**(36.0)**	**85.1**	**99.0**	**(13.9)**	**107.1**
Interest	0.6	(0.3)	0.9	0.4	0.2	3.6	(1.2)	4.8	1.9	1.7	0.0	(3.0)	3.0	3.1
Impairment	(13.9)	(18.1)	4.2	(7.1)	(6.8)	(80.4)	(132.8)	52.4	(42.2)	(38.2)	(183.3)	(205.2)	21.9	(115.6)
Exceptionals (incl BT) & Redundancy & Severance Costs	(11.3)	(14.3)	3.0	(12.0)	0.7	(118.3)	(137.6)	19.3	25.4	(143.7)	(230.4)	(216.1)	(14.3)	(157.0)
Government Grant Utilisation	0.0	0.0	0.0	18.8	(18.8)	170.0	170.0	(0.0)	148.0	22.0	170.0	170.0	0.0	316.8
Profit/(Loss) On Asset Sale	(0.2)	0.0	(0.2)	0.0	(0.2)	0.0	0.0	0.0	2.5	(2.5)	0.0	0.0	0.0	3.4
Total Profit/(Loss) Before Tax	**(19.2)**	**(22.3)**	**3.1**	**12.0**	**(31.3)**	**3.9**	**(49.2)**	**53.1**	**200.8**	**(196.8)**	**(158.6)**	**(155.3)**	**(3.3)**	**157.6**

Period vs. Budget

Operating profit (EBIT) of £5.5m was £4.8m adverse to budget.

BAU was £5.9m adverse:

- **Lower net income of £6.7m** due primarily to lower Mails, POCA and Telecoms income.
- **Higher staff costs of £0.8m** in the month. This is mainly due to Crown pay award.
- **Higher non staff costs of £2.1m**, driven by IT savings task yet to be achieved.

Offset by:

- **Lower Subpostmaster costs of £5.1m** due primarily to lower sales/ product mix.

One-off Project Costs variance of £0.4m fav.

Below EBIT

The impairment favourable variance is mainly driven by lower than budgeted capex expenditure.

YTD vs. Budget

Operating profit (EBIT) of £29.0m was £23.4m adverse to budget.

BAU was £20.9m adverse:

- **Lower net income of £31.5m** due primarily to the continuing adverse income trend; Mails (£19.7m), specifically labels, Home Shopping Returns (HSR) and Lottery, Telecoms (£9.5m), Government Services (£6.5m), mainly POCA, offset by favourable FS income (£1.6m), specifically banking, Premium Bonds and MoneyGram.
- **Higher staff costs of £2.5m** mainly due to the savings task not being achieved (£2.4m from Supply Chain and £0.6m from Commercial), the Crown pay deal and the CMA pay award, offset by a lower bonus accrual.
- **Higher non staff costs of £12.8m**, driven by the £10m provision for client compensation, impact of the centrally held savings task of £4.5m not being achieved, £3.0m accrued for Mails Segregation penalty payment, It savings task yet to be achieved and higher postage costs offset by improved VAT recovery of £11m (relating to the prior year).

Offset by:

- **Lower Subpostmaster costs of £25.5m** due primarily to lower income and sales mix (£16.8m), VAT recovery (£3.7m) and other small variances relating to NT changes.

One-off Project Costs variance of £2.4m adverse mainly due to unbudgeted project Sparrow (FYF c. £7m) and unbudgeted strategy consultancy costs.

Below EBIT

Both impairment and exceptionals are under budget due to underspends in NT, CT and IT& Change. Although lower than budget, these are both twice last year's spend. The exceptionals budget also includes £8m ATOS contract set up payment incurred in 2013-14 but budgeted for 2014-15. Government grants have now been fully utilised.

YTD vs. Prior Year

Operating profit (EBIT) of £29.0m was £36.0m adverse to prior year.

Like for like BAU adverse variance of £17.2m was mainly due to:

- **Lower Staff cost of £6.6m** driven primarily by a lower productivity bonus and Crown savings.
- **Lower Subpostmaster costs of £1.8m** which are almost flat year on year.

Offset by:

- **Lower net income of £3.5m**. The variance versus prior year is driven primarily by lower Government Services income, mainly POCA and Telecoms offset by higher Financial Services (Moneygram, Mortgages, Savings and Insurance) revenue.
- **Higher non staff costs of £23.4m** due to £10m client compensation provision this year, increased IT costs (mainly Horizon and ATOS) and higher marketing spend (including some switched from POOC) offset by improved VAT recovery.

Non like for like adverse variance of £18.8m was due to:

- Lower Network payment of £23.9m, offset by
- Lower project costs of £5.1m.

Below EBIT

Included in grant utilisation this year is £77m of 2013-14 exceptional spend for which there was insufficient grant last year.

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CFO High Level Profit Outlook At Period 7

October 2014

£'m	Income	JV Income	Staff Costs	Agents Costs	Non-staff	POOC	Costs	NSP	EBIT	Comments
Budget	**925**	**35**	**(239)**	**(491)**	**(274)**	**(17)**	**(1,021)**	**160**	**99**	
Mails and Retail										
Mails										FYF of £345m including £2m uplift for Christmas campaign
Lottery and retail										Camelot volumes IRRELEVANT; Health lottery fixed fee IRRELEVANT; Retail IRRELEVANT
Mails segregation penalty										Max penalty under MDA of IRRELEVANT assume negotiate down as in 13/14
Government Services										
POCA										Non-receipt of IRRELEVANT; one-off from DWP IRRELEVANT; IBOR
DVLA										Volume upsides on tax discs and AEI IRRELEVANT; one-off change control for EVL's IRRELEVANT
IDA										Delayed launch. Still reliant on Cabinet Office committing to volumes
Passports										Digital passports delay, partially offset by paper passports volumes and price increase
Telephony										
Homephone										Lower customer numbers and ARPU's, higher wholesale costs; partially offset by FJ claim
Mobile & Energy										Launch delayed and budget included 'stretch' volumes. Proposition not being launched this year
Financial Services										
Staff Costs										
Commercial										New Commercial structure does not deliver budgeted savings task
Supply Chain										£2m savings budgeted. IR delayed implementation of new ways of working
CTP franchising										Risk from delays to franchising
Non-staff cost savings										
Marketing										Updated October forecast which includes £3.8m for Christmas campaign
Official Mail										Cheque pouches not budgeted IRRELEVANT Passports check and send volumes IRRELEVANT
Central										
Release of contingencies										Release all of income contingency
Trading forecast at P6	**880**	**35**	**(243)**	**(466)**	**(278)**	**(17)**	**(1,004)**	**160**	**72**	
Further 'Trading' risks										
Client Compensation										
Additional Mails segregation penalty										Max penalty under MDA is IRRELEVANT assume can negotiate down as in 13/14
Agents costs										
Locals										
NFSP members subs										
Staff Costs										
Central bonus release										Bonus provision reduced from 90% to 50% payout (assumes miss ETDBW, Income, Crown profit)
Non-staff										
Additional savings opps identified										Additional opps identified by the functions against the August cost target
VAT on RM IT charges										£2.5m budget challenge achieved except VAT impact not covered
New IT services not budgeted										SSK maintenance IRRELEVANT FRP support costs IRRELEVANT Fujitsu Tier 2/3 Helpdesk £0.6m; RM Projects PY depreciation charge IRRELEVANT
IT Savings task										Savings task budgeted covered by opportunities below
IT Opportunities identified against task										£0.5m Staff Costs; £1.4m small change budget; £1.7m IT Services supplier opps; £0.8m ATOS savings
Homephone discount										£2m Horizon discount agreed as part of HPBB contract for POL not undertaking a competitive procurement.
HR costs & Communications costs										Agreed £800k 2014-15, £200k to applied to change works and £1m for 2015-16
Central task not underpinned										Savings identified from L&D budget £0.5m; offset by higher recruitment costs. Various savings identified from Comms budget
Bank charges										Budget tasks included in Central, including £1m Official Mail. Included in Central budget, not underpinned by any initiatives
Projects										Run rate risk
Sparrow										
Strategy consultancy										Full cost estimate £5.3m covering mediation on c.140 cases. Only £0.3m considered exceptional
POOC savings (FS and Commercial)										McKinseys costs already incurred for Journey to 2020 work + IRRELEVANT for FS strategy work
Central										Latest forecast from Commercial and FS. Assumes Project Wave delayed
VAT recovery rate - prior year										
VAT recovery rate - current year										Taken in H1
CONTINGENCY										Total VAT recoveries of c£30m, budget already included £7m
CFO Outlook at P6										

IRRELEVANT

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Crown Profit & Loss Statement

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October 2014

£m	Period Actual	Period Budget	Period Variance	Prior Year Period Actual	Prior Year Period Variance	YTD Actual	YTD Budget	YTD Variance	Prior Year YTD Actual	Prior Year YTD Variance	Full Year Q2 Forecast	Full Year Budget	Full Year Variance	Prior Year Outturn
Income and Distributions														
Variable income														
- Mails														
- Financial Services														
- Government Services														
- Telecoms														
Fixed income														
Gamma/ Other														
Renewals and Retentions														
Total Income including Gamma/other														
Branch costs -														
- Staff														
- Property														
- Other branch costs														
Infrastructure costs														
Allocated central costs														
Total Expenditure														
JV Share of Profits														
Statutory PBIT														

IRRELEVANT

IRRELEVANT

Summary

Income:

Income is £5.1m less than plan.

At a business level this is predominantly driven by adverse variances in Mails, including Labels, Home Shopping Returns and Lottery, Government Services and Telecoms, with a favourable variance in Financial Services.

Line by Line variances are as follows:

- Variable sales income is IRRELEVANT less than plan principally due to (i) Mails - Lower parcel volumes, Retail sales and Home Shopping Returns, (ii) Financial Services – shortfall from Life Insurance, Home Insurance and variable sales of Savings products. There is a corresponding upside in savings retention income due to the income guarantee with Bank of Ireland. Premium Bonds and Mortgages are also performing above target. (iii) Government Services – predominantly due to higher Passport check & send transactions. However, there is a variance in 'Other Income' that partially offsets this due to an element of the Passports target being held centrally in Other Income.
- Fixed income is adverse due to lower than planned LIBoR rates for Card Account commissions.
- Retention income is adverse due to a lower customer base and Averaged Revenue Per User for HomePhone, partially offset by favourable Savings retention income.
- Other income is adverse due to the delay or phasing of new products, predominantly Energy. Passport Check & Send (actual income in variable sales) is the other key driver. There was also a central Financial Services target that is held here and being delivered within Financial services variable income .

Costs:

Costs are £3.8m higher than plan.

- Staff costs IRRELEVANT adverse primarily due to timing of the roll out of Franchising and the impact of the pay review settlement where associated efficiencies will be achieved in future months, this is partially offset by Crown branches vacancies, mainly Financial and Mortgage specialist.
- Other branch costs are favourable to plan due to lower than expected losses although these may reverse in the coming months.
- Property costs IRRELEVANT adverse due to the delayed savings for the new Facilities Management contract, which started in October , however POL have not yet received an invoice from the new supplier.
- Central Costs are IRRELEVANT adverse due to a provision for client compensation, impact of centrally held savings not being achieved, accrual for Mails Segregation penalty and higher postage cost, partially offset by improved VAT recovery rates.

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Cost Management update

October 2014

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Progress since P6 update

Value and confidence

The Cost Reduction Group (CRG) has continued to drive focus on cost management and after further assessment of opportunities the gap between the in-year delivery of "line of sight" initiatives and the total cost reduction challenge has reduced to £9.2m (from P6 report of £14.9m).

Original Cost Management Programme	£34.2m
Additional Cost Challenge to achieve budget	£ 6.0m
Central Stretch to achieve budget	£ 5.9m
Total Budget Cost Challenge	**£46.1m**
Additional Challenge from Q1 EBITDAS gap	£ 7.0m
Q2 underperformance adjustment	£ 6.9m
Total Current Cost Challenge	**£60.0m**
Current "Line of Sight" forecast	£50.8m
Gap to £60.0m	£9.2m

Delivery and governance

Regular 121 meetings continue to drive focus on in-year cost management opportunities and delivery of existing initiatives. Central business wide opportunities identified during September and October including the acceleration of McKinsey identified savings have provided further potential in-year value but more ideas are required to fill the current gap to target.

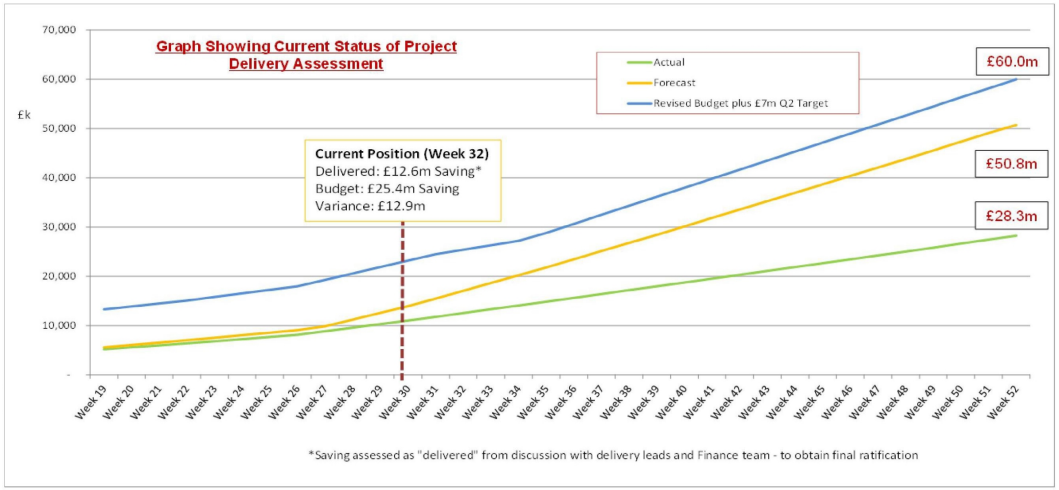
Strategic initiatives for FY15/16 and beyond

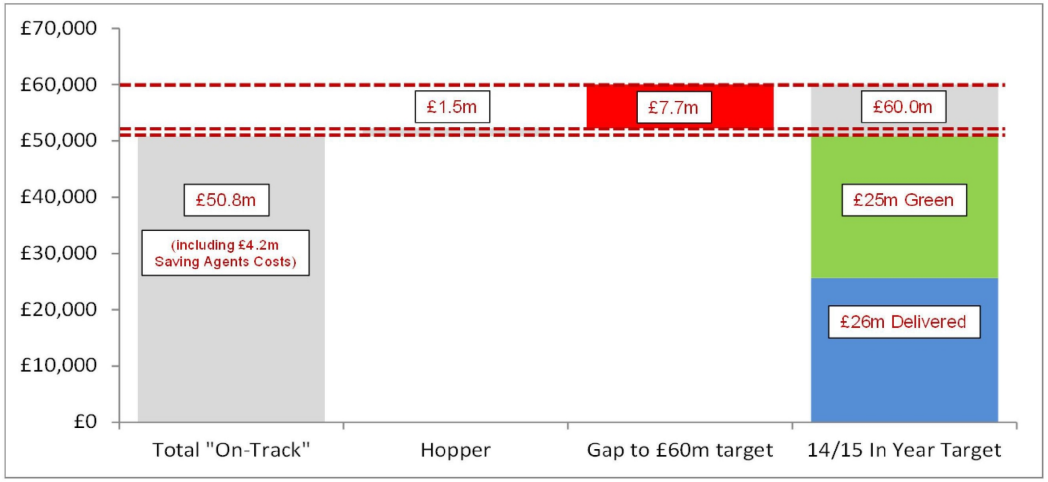
The overall Programme has progressed through Stage 3, designing the financial glidepath to 2020.

Work is ongoing to;
1) Identify a portfolio of incremental cost saving opportunities to achieve the £60m in-year improvement target placing all the cost saving initiatives under the scrutiny of the programme to ensure the expected improvement has the requisite effect on the 2014/15 EBITDAS outturn.

2) Ensure the benefits from these opportunities are sustainable in order to meet 2015/16 EBITDAS targets, moving towards £100m of sustainable run-rate saving by March 2016

3) Deliver the target operating model that will ensure the cost efficiency targets for the programme (to 2019/20) are realised;



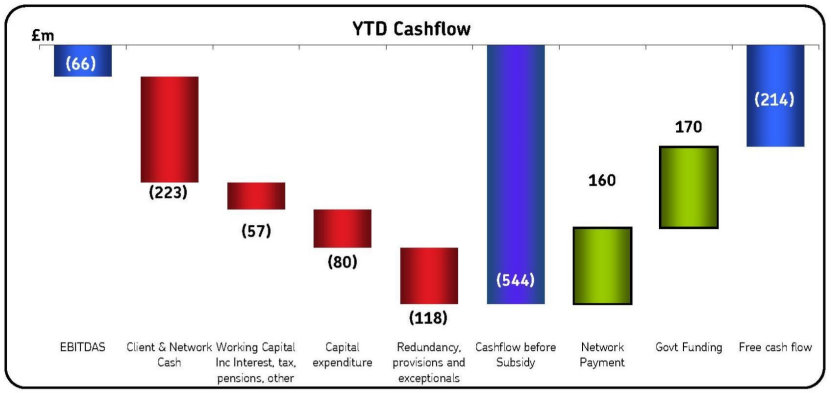


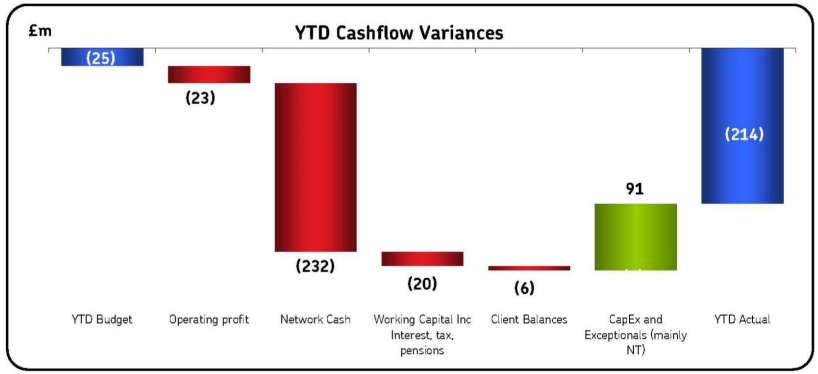
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Cashflow Analysis

October 2014





Cashflow

The £330m of government grant was received on 1st April which is the last payment of the 2010 funding agreement with BIS.

P7 cash outflow of £214m is £189m adverse to budget of £25m outflow.

The adverse variance is mainly due to:

- Network Cash was £232m adverse mainly due to cash being increased in branches (£133m adverse) and cash centres (£83m adverse) to mitigate operational impact of industrial action in Supply Chain. In addition DWP paid winter fuel payments in period 7 (usually paid in period 8). The other large adverse variance is in cheques (£23m adverse) because of higher than expected premium bond sales (largely offset by client creditors below)
- Operating profit is £23m adverse to budget.
- Working capital was £20m adverse.
- Client balances were £6m adverse comprising favourable variance from higher than expected Premium Bond (£19m) and Payout sales (£18m) offset by an adverse DVLA variance (£44m) again due to higher sales.

Offset by:

- Capital and exceptionals continue to be favourable (capital £52m and exceptionals £39) due to

Network Cash

£m	Prior Year	Mar-14 Opening	P7 Actual	P7 Budget	P7 var
Retail, Cash Centres	696	522	728	527	(201)
Bureau	70	58	68	53	(15)
Cheques, debit cards	119	129	146	131	(15)
Network Cash	**885**	**708**	**942**	**711**	**(231)**

	Opening	P7
Headroom (£m)	**854**	**975**

£m	YTD Actual	YTD Budget	YTD Variance	Q2 Forecast	Full Year Budget
EBIT	**(66.3)**	**(43.0)**	**(23.3)**	**85.0**	**(61.0)**
Working Capital	(72.1)	(56.5)	(15.6)	49.5	27.0
Client Balances	11.3	17.0	(5.7)	(3.0)	17.0
Network Cash	(234.1)	(2.6)	(231.5)	(91.6)	(57.6)
Capital Expenditure	(80.4)	(132.8)	52.4	(145.0)	(205.2)
Government funding	330.0	330.0	0.0	170.0	330.0
Exceptional Items	(117.9)	(156.8)	38.9	(213.4)	(240.3)
Other (including interest and tax)	15.9	20.0	(4.1)	(9.9)	(9.9)
Operating Cashflow	**(213.6)**	**(24.8)**	**(188.9)**	**(158.4)**	**(200.0)**

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Business Scorecard

October 2014

Strictly Confidential

Key Performance Indicators	Current Month			YTD			YTD	Full Year			2013-14
	Act	Target	Var	Act	Target	Var	Prior Year	Q2 F'cast	Target	Var	Outturn
Growth											
Total Net Income (excl NSP) £m (Bonus 20%)	77.9	84.6	(6.7)	500.1	531.6	(31.5)	503.5	880.0	925.1	(45.1)	866.7
Operating profit £m (Bonus 25%)	5.5	10.4	(4.8)	29.0	52.4	(23.4)	65.0	85.0	99.0	(14.0)	107.1
Earnings before ITDA and Subsidy £m*	(9.7)	(5.0)	(4.8)	(66.0)	(42.6)	(23.4)	(54.0)	(74.4)	(60.4)	(14.0)	(92.5)
Free cashflow £m	(236.6)	39.4	(276.1)	(213.6)	(24.8)	(188.9)	196.8	(158.4)	(200.0)	41.6	179.7
Customer											
Customer Satisfaction**	86.1%	89.0%	(2.9)%	87.1%	89.0%	(1.9)%	88.0%	87.5%	89.0%	(1.5)%	87%
Easy to do business with (Bonus 15%)**	24%	47%	(23)%	26%	47%	(21)%	44.2%	26%	47%	(21)%	41%
Net Promoter score**	3	2	1	1	2	(1)	-2	0.5	2	(1.5)	(4)
Queue time % < 5 minutes - Top 1k branches	80.1%	87.0%	(6.9)%	77.8%	83.1%	(5.3)%	84.1%	77.5%	81.2%	(3.7)%	82.1%
Branch Compliance - Financial Services - basket of 11 measures	90	<=60	-	80	<=60	-	N/A	110=> <=60	<=60	-	N/A
Branch Compliance - Inland Dangerous Goods **** ^	70.0%	80.0%	(10.0)%	70.0%	80.0%	(10.0)%	TBC	80.0%	80.0%	0.0%	TBC
Branch Compliance - International Dangerous Goods **** ^	80.0%	85.0%	(5.0)%	80.0%	85.0%	(5.0)%	TBC	85.0%	85.0%	0.0%	TBC
People											
Engagement Index % (Once a year April) (Bonus 15%)^^	58%	58%	0%	58%	58%	0%	55%	58%	58%	0%	57%
Subpostmaster Engagement Index % (Once a year)^^	47%	48%	(1)%	47%	48%	(1)%	N/A	48%	48%	0%	45%
Post Office Values the diversity of the workforce (Once a year April)^^	54%	66%	(12)%	54%	66%	(12)%	N/A	66%	66%	0%	52%
(No.) % of BME appointments over total recruits at senior leadership and senior manager	0%	7%	(7)%	9%	7%	2%	11.5%	7%	7%	0%	11%
(No.) % of Female appointments over total recruits at senior leadership and senior manager	33%	45%	(12)%	40%	45%	(5)%	53.8%	45%	45%	0%	46%
Modernisation											
Crown Profit (Loss) £m	(1.5)	0.5	(2.1)	(14.2)	(5.4)	(8.8)	(11.9)	(13.8)	(8.9)	(4.9)	(25.7)
Crown Profit (Loss) Run Rate £m (Bonus 12.5%)^	N/A	N/A	N/A	(11.7)	(6.7)	(5.0)	N/A	(2.0)	0.0	(2.0)	N/A
NT Transformations - contract signatures ***	0	144	(144)	4,168	3,944	224	2,113	4,800	4,800	0	3,246
NT Branches Transformed In Year (Bonus 12.5%)	0	140	(140)	1,076	996	80	295	1,650	1,650	0	1,551

Bonus worthy metrics

* ITDA Interest, Tax, Depreciation, Amortisation.

** Monthly = 3 month average. YTD = 12 month average.

*** YTD and FY = cumulative including prior years.

**** POL are looking to hit 100%, and these target have been set for 2014-15 in recognition that marked improvement is required to reach 100%.

^ Target is the year end exit rate.

^^ Measured annually with some additional 'Pulse surveys'.

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Network Transformation Scorecard - Mains

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October 2014 Reporting prior months data (i.e. one month in arrears)

	Key Performance Indicators	Current Month % Actual	Control Group	Var	Ave £'s per branch Var	Actual Sample Size
POL	Finance Approved Investment per Mains £000	(42)	(42)	0	0	
	Total Income: Post vs Pre Conversion					
	Branches live 6-12 months	4%	(1)%	5%	382	547
	Branches live 12-24 months	(1)%	(6)%	5%	388	552
Agent	**Agents Remuneration: Post vs Pre Conversion**					
	Branches live 6-12 months	4%	(4)%	8%	518	547
	Branches live 12-24 months	6%	(4)%	11%	812	552
	Customer Sessions					
	Branches live 6-12 months	1%	(3)%	5%		492
	Branches live 12-24 months	(0)%	(5)%	4%		466
	Operator Feedback on Retail Sales Performance	7%				155
	Operator Satisfaction	81%				73

		Actual	Target	Var	Actual Sample Size
Customer	Average Increase in Opening Hours	41%	20%	21%	1,550
	Customer Satisfaction	98%	90%	8%	30
	Queuing Times	1m 24s	< 5 mins	3m 36s	190

Mains

Branches that have been converted to a Mains model for more than 6 months have consistently out-performed the control group in delivering POL income. These agents receive a dedicated package and a renewed focus on sales targeting and performance at the point of conversion. This is having a significant impact on focus income for many branches.

The following products are performing particularly well:

- Travel insurance
- Passport check and send
- Cash withdrawals
- Growth bonds
- Insurance products

In addition, these agents have increased their POL earnings due to the improved sales and enhanced Mains pay rates.

Note: the control group is based on those branches of similar size that have not yet converted.

Customer

Customer Satisfaction, extended opening hours and queue times all remain positive.

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Network Transformation Scorecard – Locals

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October 2014 Reporting prior months data (i.e. one month in arrears)

	Key Performance Indicators	Current Month % Actual	Control Group	Var	Ave £'s per branch Var	Actual Sample Size
	LOCALS					
POL	Finance Approved Investment per Local £000	(11)	(11)	0	0	
	Total Net Impact: Post vs Pre Conversion					
	Branches live 6-12 months					
	Income	(6)%	(5)%	(1)%	(16)	240
	Actual Fixed pay savings				930	
	Actual Net impact				914	
	Branches live 12-24 months					
	Income	(10)%	(11)%	1%	26	183
	Actual Fixed pay savings				919	
	Actual Net impact				945	
Agent	Customer Sessions					
	Branches live 6-12 months	10%	(2)%	12%		130
	Branches live 12-24 months	7%	(3)%	11%		190
	Operator Feedback on Retail Sales Performance	16%				52
	Operator Satisfaction	79%				56

		Actual	Target	Var	Actual Sample Size
Customer	Average Increase in Opening Hours	111%	80%	31%	1107
	Customer Satisfaction	95%	90%	5%	30
	Queuing Times	55s	< 5 mins	4m 05s	274

Locals

At the point of conversion there is an initial decline in performance; as the branches settle and embeds the operational changes. However this improves month on month and as they near the exit of the 6-12 month category the run rate of performance is now higher than the control group. This is partially as a result of the activities that have been put in place to limit the drop off in income and drive performance. Although the impact on the Locals due to NS&I is still having an adverse effect on performance the underlying trend of other products is showing an improvement.

As the better performing branches move through the categories this is reflected in the 1% increase in performance for the 12-24 category

Customer sessions/footfall continues to be strong so this should support the agents retail growth.

Note: the control group is based on those branches of similar size that have not yet converted less 5% to reflect lost products.

POL

- Products such as bill payments, etop ups, cash withdrawals and MoneyGram have delivered growth for these branches – with associated footfall. This has been offset in income terms by poorer performance on more complicated products.
- Fixed pay has been reduced to zero for all converted branches, in line with the strategic plan.
- On average Lottery income has reduced by c. £60k p.a in these branches. Corrective action on how we minimise future risk is now being looked at, principally by improving the sales messages and focus of the FCA's when signing up the retailer as well as the LRM's focussing on these messages for those already converted

Agent

- Customer sessions indicate that retailers are benefiting from greater footfall that should support their retail growth.
- The footfall is delivering quicker but lower value Post Office sales which in turn should allow the retailer to utilise their staff in different ways or reduce their staff costs.

Customer

- Customer Satisfaction, extended opening hours and queue times all remain positive.

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Transformation Overview

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October 2014

- RAG, cost and benefits based on full programme life
- RAG in brackets indicates programmes view
- Overview used as part of Board Pack to update Board on Transformation progress

- **New Transformation Portfolio category added to show status of the delivery of the 2020 EBITDAS strategic plan proposed in Business Transformation Design phase. After we have implemented the Transition Plan this category will summarise the position across all programmes under the new Roadmap**

Programme	Time	Cost	Benefit	Quality	Comment / Areas for Discussion
Business Transformation **(Design Phase only)**	G	G £7.5M 14-15	N/A (A)	A (G)	The design phase will be complete by the end of November having delivered an 'end state' operating model design and transformation 'blueprint'. Transition business cases are now being prepared to manage the transition from a 'design' to a 'delivery' structure and operational efficiency accelerators. Final recommendations will be made to the Board in November to secure approval for transition into delivery. Quality measures amber status as quality measures not yet achieved.
Winning in Mails	A	A (G)	R	A	The Ivy pilots continue to roll out but usage remains extremely low. Digital marketing has been implemented and a range of other marketing and PR activities are underway to drive up Home Shopping Returns volumes. The greatest challenge for the programme remains securing support from Royal Mail at the required pace. As the Board is aware, there was a Chair-to-Chair meeting between RMG and POL to secure this support where two shared workstreams were agreed: firstly, to map out the costs savings for both organisations from customer journey simplification; and secondly, a joint commitment to secure a network with a major retailer such as McColls. On the first workstream, agreement has been reached between POL and RMG on the specifics of what needs to be delivered to support the extended trials, namely product simplification (to allow removal of weighing scales), changes to operational requirements (no segregation of parcels and RMG collections at the new sites) and requirements for the technical solution. Work is progressing to understand where there is potential to remove costs from both organisations – on the basis of simplification and changes to operational process. To the second workstream, the commercials for an interim deal with McColls remain to be agreed and are expected to conclude by the end of November. However, this step is critical as it will crystallise the cost implications of the above changes for both businesses, upon which the operational agreements are dependent. Following commercial agreement, we expect to secure an MOU with McColls by mid-December.
Network Transformation	A	A £956M	G	G	The programme remains ahead of target on both contracts and openings. Transitional locals are progressing without significant adverse stakeholder reaction although the workstream is time-consuming as decisions need to be made on a case by case basis. The value for Money workstream has identified potential cost savings that will be investigated further by the Business Transformation programme. Discussions on the cliff are starting with the NFSP and co-ordinated via the P&E team.
Crown Transformation	G	G £126M	R P&L Break Even	G	The programme continues to deliver in line with targets across branch transformations, training (>3000 staff trained), staff cost reductions (>470 FTE), SSK rollout (>480 rolled out), mergers and relocations - though current P&L run rate at year end is forecasting a £2M loss primarily due to a £7M income shortfall. Quality measure moved to green status as customer satisfaction continues to improve, with both overall satisfaction and queue time satisfaction meeting (or very close to) target.
Branch Support	A	G £8M	A £3M P/A	G	Enterprise Case Management recommendations yet to be agreed at Business Transformation Steering group, once outcome is known impact on Branch Support benefits will be recalculated. Activity to realise savings (C.£284K) from online training, brought forward from next financial year are in flight and are aligned with the HR1 processes across Business Transformation.
IT Transformation	A	R £53M	A £25M P/A	TBC	Fujitsu have informed Post Office that they are withdrawing from the Front Office procurement process. The programme has initiated a full impact assessment, with a specific focus on managing the risk around continuity of service. Discussions have commenced with Fujitsu to de-risk the Front Office execution by extending the contract beyond March 2017. The initial view is that a 12 months extension is required; however this is being tested considering the commercial impact. The Board will have the opportunity to review the programme in January. The updated Business Case shows an increase in transition costs and the programme is working with the finance team to minimise the exposure and to agree the most appropriate way to secure the funding. The increase is largely due to more informed bidder responses to the procurements and changes to assumptions in the original estimates for the Network tower. The latest costs and assumptions have been used in the Business Transformation Roadmap and financial glide path. Mobilisation of the EUC delivery team is underway following the award of contract.

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Transformation Overview

October 2014

- RAG, cost and benefits based on full programme life
- RAG in brackets indicates programmes view
- Overview used as part of Board Pack to update Board on Transformation progress

Programme	Time	Cost	Benefit	Quality	Comment / Areas for Discussion
Separation	G	A £44M	N/A (G)	G	The programme is delivering against the revised timeline within the MSA Extension Letter, with significant milestones approaching before the end of the calendar year for Contact Centres, and ebusiness and Networks by the end of the financial year. A key enabler for eBusiness separation has recently been achieved with customers requesting the www.postoffice.co.uk website now being served content and tools from Post Office rather than Royal Mail. The majority of the business services have now been separated, with all the remaining IT ones planned to be separated by the end of quarter 2 2015.
Titan	A	G	G	TBC	Update reflects whole programme but will move to Post Office only deliverables (rather than POMS) from December to ensure clear lines of governance. Contractual relationships with third parties for distribution and servicing progressing slightly behind plan but programme anticipate all will be completed within timescales. Key risks that PO board do not give authority to trade due concerns over readiness, and FCA do not provide authorisation within required timescales. Contingency plans being developed for both to enable uninterrupted Travel Insurance sales. Costs and benefits forecast inline with business case.
Hawk	N/A as in negotiation phase				IRRELEVANT
Investments and Savings Negotiations	N/A as in negotiation phase				
FS Sales Effectiveness	A	G £1.5M 14-15	A	TBC	This Programme has been set up to achieve break-even sales volumes in 2017/18 (10 sales per week per specialist as presented in the FS Strategy at the September Board) and then go on to deliver 15 sales per specialist per week by 2020. Phase 1 of the "Post Office Money Academy" is due to go-live in support of broader Post Office Money sub-brand launch. Priority training modules are on track but LMS (Learning Management System) is still in design. We are working with L&D colleagues to launch with an interim solution.
Post Office Card Account (POca)	A	G £0.28M	A	TBC	The Public Procurement project is currently on track. POL and DWP are working to conclude the BAFO (commercial discussions on the content of the extended POca service) in support of the Ministerial announcement (end of November). The OJEU will commence shortly after this decision. Contract award and implementation commencement are scheduled for end of Q3 15/16. However, the overall RAG status for the continuation of the POca service is Amber for Time (the impact of slippage to the Ministerial announcement causes a potential risk to the start of the new supplier service in April 2017). Benefits are Amber due to the uncertainty regarding DWP decision to either extend the existing contract for 2 years or commit to a 7 year continuation. Quality metrics are to be confirmed with the project.
Mobile Proposition (Wave)	G	R £4.5M	A	TBC	Cost challenge has impacted on original timescales/benefits and has led to re-planning of key milestones and re-phasing of benefits. 'Friendly user trials' are currently on track for January 2015 and the National launch of pre-paid and pay monthly is now scheduled for Q2 and Q3 2015 respectively. Cost status is Red due to the enforced delay which has extended the programme timelines and increased overall costs - an increase of £300k is currently forecast. Benefits status is Amber as income generation is delayed until 15/16. Quality metrics are to be confirmed with the project.
People & Engagement					The People and Engagement strategy and detailed actions for the next 12-18 months have been agreed by ExCo and the Board. The actions within the plan are aligned to the accelerators and are underpinned by the business approach to risk management. Short term focus will be on: 1, Stakeholder management (inc. NFSP, TUs, RMG, BIS) 2,Supply Chain strike ballot closing on 18th November 3, Business Transformation Wave 1 activity and management OD

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POST OFFICE LTD

Post Office and the Bank of Ireland Relationship

1. Purpose

1.1 This paper provides an overview of Post Office's relationships with the Bank of Ireland UK plc (BoI), setting out the key risks and the controls and mitigating actions that we either are deploying or can deploy and actions for the future.

1.2 The Board is asked to note the paper.

2. Summary

2.1 The Post Office – BoI relationship spans a wide range of businesses, viz:

- Personal Financial Services, through the Financial Services Joint Venture Agreement ("FSJVA" or Eagle), which currently encompass:
  a) Savings
  b) Mortgages
  c) Credit cards and personal loans
  d) Current Account, and
  e) General & Life Insurance
- Business and personal banking;
- ATMs;
- Travel money (through the First Rate joint venture);
- Travel insurance (regulatory cover only); and
- IRRELEVANT not in FS).

2.2 In 2014/15 these businesses will generate revenues (including FRES profit share) to Post Office of IRRELEVANT

2.3 The relationship established through Eagle was born out of the need to IRRELEVANT oint venture that was generating limited value to Post Office. That agreement exposed Post Office to risks it could not mitigate (e.g., IRRELEVANT and put Post Office in the position of a channel provider rather than partner. The FSJVA addressed these issues and established a more effective and clearer relationship.

2.4 The FSJVA was not able to remove the space for disagreement and dispute between the parties but it gives Post Office much greater control and an ability to require BoI to meet its obligations.

3. The relationship today

3.1 Over the past year as BoI has become more financially stable, aspects of the strategic aims of the parties have diverged IRRELEVANT IRRELEVANT This can be seen in IRRELEVANT IRRELEVANT and restructuring of its balance sheet (to IRRELEVANT These actions have typically bee IRRELEVANT IRRELEVANT

3.2 The strategic divergence highlights two in-balances in the relationship, viz:

- The divergence between the size of IRRELEVANT Post Office's customers; and

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- The significantly higher IRRELEVANT

3.3 Post Office FS now believes we have reached a point where we need to either

IRRELEVANT

3.4 The intent of a challenge would be to bring BoI back into alignment with the agreed strategy.

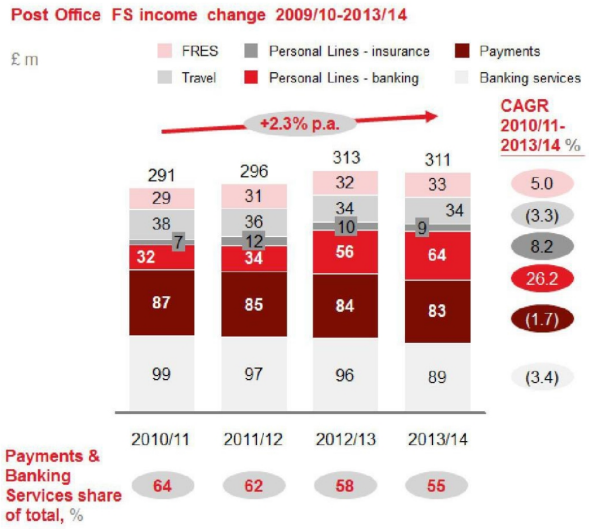
3.5

IRRELEVANT

The FSJVA

3.6 Since the establishment of Eagle the Post Office has experienced a significant uplift in revenues and focus in BoI and Post Office on developing financial services. Table 1 highlights that FSJVA related income rose from IRRELEVANT (2009/10) to IRRELEVANT (2013/14), with a target of IRRELEVANT in 2014/15.

Table 1



3.7 Some of the key successes that jointly we have delivered together include: the creation of a qualified mortgage specialist sales force meeting the new MMR requirements along with breaking into the mortgage market as a new provider; delivering a leading online credit card application process; reengineering a number of product processes; winning a significant number of industry awards; establishing positive Net Promoter and Customer Effort scores; and building an effective cross-party conduct risk and compliance capability.

3.8 However there are a number of areas of strategic concern and the following sections provide an overview of the status of each core product:

3.9 Savings – this has been the leading business for Post Office with BoI, with an agreed plan for 2014/15 to reach a book of £18 billion[1] (and a goal of £30

[1] Generating £51 million income to Post Office in 2014/15.

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billion by 2020). Concurrently BoI has sought to IRRELEVANT IRRELEVANT

3.10 To manage these divergent requirements in October 2013 the parties agreed a plan that enabled BoI to manage its needs while meeting Post Office's short and medium term financial targets, in particular:

a) Post Office to receive a minimum IRRELEVANT in 2014/15 (delivered);

b) Post Office would support BoI IRRELEVANT

c) BoI would provide pricing to support achieving an IRRELEVANT IRRELEVANT, based on an agreed mix of variable, on-line and fixed products;

d) BoI commitment to IRRELEVANT IRRELEVANT;

e) Liability balances would grow at IRRELEVANT

f) The parties would develop online capabilities to make up any shortfall.

3.11 IRRELEVANT

3.12 Balances are now projected to be IRRELEVANT at a mix focused on fixed and on-line, rather than branch variable sales[4]. This would have a material impact on Post Office revenues in 2015/16 (c£6-7 million) and subsequent years.

3.13 We engaged with BoI to seek agreement on an interim solution while a longer term solution is developed that enabled Post Office to meet its financial targets and BoI its balance sheet flexibility. While BoI initially supported this approach, it now has declined to proceed.

3.14 Post Office is therefore moving to IRRELEVANT IRRELEVANT IRRELEVANT (a central requirement of the FSJVA).

3.15 In addition in February 2014 BoI IRRELEVANT without Post Office agreement; this is a breach of the terms of the FSJVA. We have raised this matter with BoI and reserved our rights.

3.16 Investments - The proposed move into investments was developed to provide a competitive customer solution, while reducing the reliance on BoI's balance sheet. We have unfortunately been unable yet to agree a commercial approach with BoI, with an apparent unwillingness to focus on this (seen as a distraction from its core business). This will be held over IRRELEVANT IRRELEVANT

3.17 Mortgages – whilst the establishment of the Mortgage Specialists capability in February 2014 has been successful, in July customer began to experience IRRELEVANT

3.18 The IRRELEVANT have resulted in BoI IRRELEVANT IRRELEVANT

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2 Critical to enable IRRELEVANT

3 This was structured to encourage Post Office to invest and build mortgage sales capabilities, while enabling increased liability capacity.

4 Branch variable generate IRRELEVANT

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3.19 Post Office's own branch sales performance (mainly from lead generation) needs to improve.

3.20 Credit cards, personal loans and current accounts; while there are inevitable day-to-day issues these are generally working well, although there are delays in launching products.

3.21 Insurance – through project Hawk, Post Office is exercising the option to buy out BoI's interest in insurance. The target is to conclude agreement by end March 2015. BoI has indicated that it is keen to retain involvement in insurance and we will assess a proposal. Early indications are that it is unlikely to meet Post Office's needs.

3.22 Service delivery - The Post Office-BoI Customer Delivery Forum conducts a quarterly IT Stability review of IT incidents, customer impact, root causes and determine whether there are concerning trends in systems or process breakdown that warrant investment.

3.23 While this relationship generally works well and is collaborative, recent BoI customer service has incurred a higher than usual volume of incidents. Post Office has requested that BoI conduct a more detailed review of the incidents and supporting network architecture to understand the root causes.

3.24 **ATMs**

3.25 The business relationship is working well, although with the contract due to expire in 2022 and ATMs having an eight year lifespan, BoI is less incentivised to invest – BoI has advised that it is keen to extend the agreement. Post Office is reviewing its options but much of this is dependent on the wider strategic development in the network and FSJVA outcomes.

3.26 **Personal & Business Banking**

3.27 This is a small part of the Post Office's banking services business and is working well.

3.28 **Travel Money**

3.29 The travel money relationship is effective, with BoI being largely an investor in the FRES joint venture.

3.30 We are, however, reviewing the commercial agreements as there is an imbalance between the net revenues to Post Office and BoI. We are reviewing our options and are preparing proposals to present to FRES and BoI in 2015.

3.31 Post Office is also looking at the options for IRRELEVANT IRRELEVANT and would require Post Office Board approval prior to any such engagement.

3.32 **Travel Insurance**

3.33 BoI provides regulatory oversight for the travel insurance business, and has been supporting the move to establishing POMS.

3.34 IRRELEVANT

3.35 Post Office Supply Chain IRRELEVANT IRRELEVANT Post Office also partners BoI in mainland UK through IRRELEVANT and ATM replenishment to c.100 BoI ATMs. There is a possibility that Post Office will also replenish ATM as an alternative to their IRRELEVANT

4. Post Office FSJVA controls

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4.1 The agreement with BoI is exclusive and runs at least until 2023[5].

4.2 Each party has clearly defined roles with Post Office leading on delivering an effective sales network, creating and delivering marketing and sales strategies and activities (including direct marketing and retention) and ensuring that all products and services (including all customer interactions) meet Post Office's brand requirements.

4.3 BoI leads on manufacturing products to agreed specifications, providing on-going servicing of the product (e.g., sending statements, paying interest, managing the customer's account, making sure the systems work etc.), developing pricing that meets the agreed benchmarks to deliver the business plans, providing Post Office with the regulatory requirements for marketing and selling products and managing 3rd party product provider contracts.

4.4 In return for granting exclusivity, BoI has an obligation to manufacture products Post Office requires and to meet the standards for those products to enable us to compete in the market and achieve the agreed plans.

4.5 BoI also has a duty to ensure that, as far as reasonably possible, no limitations on the growth of the Post Office book are imposed as a result of the actions of BoI on non-Post Office products. It appears that BoI is failing to meet this requirement.

4.6 Material failure by either party to meet any of the terms of the FSJVA can give rise to a formal dispute and a requirement to make good the failure. Ultimately, if not resolved this can lead to a termination event.

4.7 Additionally, BoI has to meet various prudential requirements, put in place to reduce Post Office's exposure to BoI getting into financial difficulties. Since 2012 BoI has consistently improved its financial condition and meets those requirements.

5. 2023

5.1 The agreement runs to IRRELEVANT with either party able to give IRRELEVANT year's notice from IRRELEVANT

5.2 If Post Office intends to IRRELEVANT it may announce and IRRELEVANT For market stability purposes Post Office must not IRRELEVANT IRRELEVANT

5.3 However, it is becoming clear that BoI is getting concerned about IRRELEVANT particularly if Post Office were to IRRELEVANT In such a scenario, BoI feels it would be IRRELEVANT IRRELEVANT

5.4 However, there are contractual obligations on BoI to not allow IRRELEVANT IRRELEVANT the management of the business. It is conceivable, given all of the challenges we are now experiencing that IRRELEVANT IRRELEVANT Whilst understandable, if this is the case BoI may find IRRELEVANT

6. Risks

6.1 With such a wide ranging relationship there is a risk that BoI may respond to Post Office raising an FSJVA dispute by applying pressure in other aspects of the relationship or raise a counter dispute (eg Post Office having less than 100 mortgage specialists in place).

[5] Except insurance which expires in 2020 unless Post Office completes its option.

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6.2 There is a risk that BoI may seek to withdraw its interim support for the travel insurance business. BoI however has a regulatory obligation which would make this difficult; Titan also has contingencies in place.

6.3 There is a risk that BoI may seek to slow down the Hawk project. However, the contractual process is already in train and Post Office has the right and ability to force the pace.

7. Next steps

7.1 It is proposed to initiate a dispute in relation to the management of the savings business with a view to concluding at a minimum a one year interim arrangement. This would secure Post Office's position for 2015/16 while giving the parties time to agree a new long term structure.

7.2 These negotiations would also assess the requirements to manage through the challenges from the IRRELEVANT implications on BoI's Treasury operations.

7.3 In the meantime management would seek to develop the investment strategy, while concluding Hawk.

8. Recommendation

8.1 The Board is asked to note the paper.

Nicholas Kennett
Director, Financial Services
November 2014

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POST OFFICE LTD BOARD

Project Titan and Post Office Management Services (POMS) review of preparedness by Grant Thornton

1. Purpose

The purpose of this paper is to assist the Board in making its decision on commencement of trading of POMS, with a commentary on the Grant Thornton (GT) review, of which a summary is attached, with the full version becoming available in the reading room from 24th November.

2. Background

The Board will remember that at its meeting on 26th October meeting, Nick Kennett, Financial Services Director, and Paul Havenhand, General Manager POMS delivered an update on the insurance transformation programme. It was agreed at that meeting that the GC would provide an update to the November Board on POMS preparedness for 'go live'.

It was originally envisaged that the final version of the Grant Thornton review would be available for dispatch along with the board papers on 20th November. In the event, however, its production was delayed to enable Grant Thornton to review the most recent evidence available from the project team.

A summary of their report is attached (as at 21st November) and they have agreed to provide an oral update at the Board meeting should there be any significant subsequent developments.

3. The Grant Thornton Review

The risk team engaged Grant Thornton to undertake a review of the project teams' work to the extent it related to matters relevant to operating in an FCA regulated environment. The review areas were quite wide ranging covering governance and risk management as well as important points of regulatory detail such as risk transfer agreements and policies the regulator would expect to see in place.

The review was largely based on interview and sample checking undertaken in early October, with an updated "re-review" as at 21st November.

The attached summary shows the position both as at October and as at November 21st. Progress has been made on the majority of the items reviewed in October and further concentrated effort is required by the project team to deliver these components for soft launch (Travel Insurance renewals 8 December) and hard launch (new Travel Insurance business 1 January 2015).

Whilst all of the components reviewed by GT are required for operating in a regulated environment, GT assessed items as either 'critical' or 'essential' for soft launch. For this purpose the definitions are;

Critical - soft launch cannot proceed unless the component is in place

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Essential – soft launch could proceed without the component fully in place but would require significant Board oversight and action, analysis, testing and/or development immediately post-launch.

In addition, Grant Thornton includes in their overview the statement '**the Project is now at a point where equal attention needs to be given to a holistic view of POMS, that considers how the entity will operate as a unified whole in an FCA-regulated environment. For this reason, our overarching recommendation is that the POMS' directors must continue to increase their level of engagement, to ensure that the POMS Board and its committees formulate and deliver the strategic objectives of the business supported by a suite of insightful MI that is explicitly linked to POM's evolving risk management framework'.**

We would agree that further work is required on governance and risk management including the overall control and reporting structures so it is clearer how this will work within the Post Office.

The balance of the report is largely self-explanatory.

4. Key Risks/Mitigation

The risks of going live have been extensively discussed by the Board and the FSSC. We have received no substantive feedback from the FCA on the authorisation application that was submitted on 31 July 2014. So it appears likely that the regulator may take up to its maximum permitted time, i.e until 31 January 2015, to make a decision on authorising POMS. In the interim, the POMS contingency plan will be instigated. That is to use an alternative FCA regulated firm 'Thistle' to act as the regulated Principal of POMS until authorisation has been received for POMS.

This does mean that any regulatory risk in respect of TI renewals in December will be owned by 'Thistle' but Post Office will still carry the customer and reputational risk of any failings (similar to the current position with the Bank of Ireland).

Assuming authorisation is received, POMS will then carry the regulatory risk and in the very worst case scenario, the Approved Persons (Directors of POMS) could be liable to regulatory censure including fines.

Similarly, not going live also involves risk in that the immediate implications of a delayed soft launch are that travel insurance renewals of annual policies coming up for renewal in December (c6000 policies) will not be issued because there will be no regulatory structure in place; as well as the potential loss of financial benefits in delaying the launch.

5. Next Steps

The Grant Thornton review has focussed on POMS preparedness to "go live". As can be seen from the report (page 6) there are four 'Critical' matters marked as amber that will need to be closed out (to green) before the project can go live.

The Titan Team is continuing its intensive programme to prepare for a live date early in December 2014. As a result, it is expected that further progress will have been made over the days next 10 days against the areas Grant Thornton has indicated need additional focus.

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The Risk, Titan and GT teams are working closely to resolve these issues and ensure that the 'go live' decision can be made within the required timelines.

6. Recommendation

It is recommended that the Board:

- Notes this paper and the GT summary conclusion; and
- Delegates the making of a final "go live" decision to an appropriate ad hoc Committee in early December (eg comprising the POMS Board, the Post Office CEO and a Post Office non-executive Director).

Chris Aujard
General Counsel
21 November 2014

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This version of the report is a draft. Its contents and subject matter remain under review and its contents may change and be expanded as part of the finalisation of the report.

Post Office Managed Services Ltd (POMS)

Protect Titan Review

As at 21 November 2014

Jon Sperrin
Partner
T GRO
E GRO

Mark Davies
Associate Director
T GRO
E GRO

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Our reference: JS/MJD/POMS-Project Titan/141121

Financial Services Advisory
Grant Thornton UK LLP
30 Finsbury Square
London
EC2P 2YU

T + GRO
F + GRO
DX 2100 EUSTON
www.grant-thornton.co.uk

The Directors
Post Office Limited
148 Old Street
LONDON
EC1V 9HQ

For the attention of Messrs Chris Aujard, General Counsel and Nick Kennett, Director of Financial Services

21 November 2014

Dear Sirs

Project Titan Review

We have pleasure in enclosing our draft report in relation to our review of Project Titan.

We have undertaken this work in accordance with our Terms of Engagement dated 13 October 2014.

If you have any queries regarding this report, please contact me on GRO or Mark Davies on GRO

Yours faithfully

Jon Sperrin, Partner, Financial Services Group
for Grant Thornton UK LLP

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Our approach

Purpose

This report sets out the findings of our review of Project Titan. It assesses POMS' preparedness for a 'soft launch' in early December 2014, and a full launch on 1 January 2015.

Our Approach

Our findings are based on a series of high level interviews with key project stakeholders and a limited review of selected documentation. The specific criteria and documents you asked us to review were set out in our Letter of Engagement dated 13 October 2014. In this report we refer to those criteria as 'components'.

In preparing this report we have **not** undertaken detailed testing to provide assurance that all of the current and prospective risks to which Post Office Limited and POMS could be exposed have been identified and/or mitigated. Rather, you required our review to highlight potential deficiencies or areas for improvement within the specific components you identified. We make appropriate recommendations in this report for resolution, next steps or further testing in each of those components.

Where appropriate, we highlight any obvious gaps we identified, during the course of our interviews and the documents you asked us to review, in POMS' preparedness. Where relevant we provide industry best practice recommendations that may enhance Project Titan.

The context of our ratings

Project Titan is currently 'in flight', with a number of work streams running concurrently. This is firmly reflected in the rating factors that we have used to evaluate each of the specific components you asked us to consider. We use the following rating methodology in this report to provide our view of the likely **degree of effort** required if Project Titan is to meet its soft and full launch objectives:

Rating	Definition
	Component appears on-track for launch, subject to our recommendations being implemented. Actions are either in place or in plan. There is evidence the component will be delivered and signed off by relevant stakeholders
	Launch can be achieved subject to our recommendations being implemented, but the component requires focused effort. Component may be in plan, but there are concerns over the Project's ability to deliver within the time frame, stakeholder sign-off has not been obtained and/or evidence relies solely on answers provided by the Project Team in interview, ie progress has not been validated or tested, or there is insufficient documentary evidence.
	Component requires significant development pre-launch. Rating may apply where evidence was not found, not in plan, or the plan is unrealistic.
	Component is not expected to be ready for launch or fundamental elements are missing.

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Our reporting format

Reporting format

This report sets out our findings for each of Project Titan's components. Our assessment of each component has two parts; 'Overview' and 'Key Issues'. These are described below.

Overview

Sets out our overall findings for each component to arrive at an overall rating of POMS' preparedness to go live as follows:

Component description	Our overall findings	The evidential basis of our findings	Overall Status	Criticality
Description of the component under assessment and what we would expect to see at 'go live'.	High-level overview of our findings based on the information provided.	Commentary on the level and quality of information relied on at the time of our review and the level of information provided to validate statements made in interview. One of three criteria: • interview only • interview and documentation review • documentation review only.	Overall rating for the component based on the definitions in slide 4. Where the evidential basis is interview only this may impact the rating, since more work may be required to demonstrate or validate progress.	Overall rating of whether the component is: **Critical** - soft launch cannot proceed unless the component is in place **Essential –** soft launch could proceed without the component fully in place, **but** would require significant Board oversight and action, analysis, testing and/or development immediately post-launch.

Key issues identified

Sets out key individual issues identified within each component, observations on the potential impact of those issues, and our recommendations for action. The number and materiality of issues may vary between components.

Issue	Impact/observation	Resolution/action required	Issue Status
Description of the issue identified. Could be a confirmation the element is in place, or an identified gap requiring action.	Description of completed and planned actions and our commentary and observations on the effectiveness of those actions.	Our recommendations for action(s)	Overall rating for the individual issue based on the definitions in slide 4 and commentary in "Overall status" above.

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Executive Summary

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Overview

Our overall view is that Project Titan requires focused effort to be ready for soft launch.

Of the twelve components reviewed we rated:

- Four as 'Critical' and 'Amber'. Soft launch can be achieved subject to our recommendations being implemented, but the component will require focused effort.
- Five as 'Critical' and 'Green'. These components appeared to be on-track for soft launch subject to our recommendations being implemented.
- Three as 'Essential' and 'Amber'. In these instances soft launch could proceed without the component being fully in place and embedded, **but** the component will require significant Board oversight and action, analysis, testing and/or development immediately post-launch.

Our overall ratings for each of the components we assessed are set out in our "Summary overview" overleaf. For comparison, the Summary overview sets out our ratings at 24 October 2014 alongside our ratings as at 21 November. This comparison illustrates the progress the Project Team has made. The ratings should be considered in line with our approach and reporting format described on pages 4 and 5. In the body of this report we set out our detailed findings, and make recommendations to help the POMS Board demonstrate that Project Titan will be ready for soft launch.

Out of necessity Project Titan has been principally task-focused. In common with all large scale projects there are many interconnecting dependencies and a significant reliance on third parties performing in line with expectations and/or contractual obligations. In some areas delays in finalising contractual terms have had an impact on core deliverables. For example, at the date of this report the agreement with the insurer underwriting POMS' products had not been signed. Whilst this may be a straightforward administrative matter any delays to contract completion, or in the worst case scenario insurer withdrawal could have a materially disruptive impact on the Project.

The scale and pace of the Project may have led to a focus on resolving individual issues. Whilst this is understandable, the Project is now at a point where equal attention needs to be given to a holistic view of POMS, that considers how the entity will operate as a unified whole in an FCA-regulated environment. For this reason, our overarching recommendation is that the POMS' directors must continue to increase their level of engagement, to ensure that the POMS Board and its committees formulate and deliver the strategic objectives of the business supported by a suite of insightful MI that is explicitly linked to POM's evolving risk management framework. The FCA will expect to see the cultural 'tone from the top' being clearly set early, so that POMS is able to tangibly demonstrate that customers are placed at the heart of the business from the outset. We note that this engagement has increased over recent weeks, and have seen evidence that POMS Board oversight and activity is intensifying now that Project Titan has transferred into POMS.

We also draw the POL Board's attention to the following observations that could impact delivery of the project:

Key person risk

The scale of the project means there are a number of tasks that need to be completed in a short timeframe. Some of these tasks are likely to be relatively straightforward to execute in isolation. However, in aggregate there is a material volume of outstanding work that needs to be completed. A key observation of our review is that Project Titan is critically exposed to key person risk. During our review we formed the view that Richard James and Russell Weekes are extremely capable experts. However, both are consultants rather than full time POL employees. If either or both of these key people were unavailable the project could slip quickly, particularly if the pace of the project has meant that knowledge transfer has been limited. Given the project is about to enter a crucial phase we recommend the POMS Directors formulate a clear plan to manage this risk in the event that it crystallises.

Delays in FCA authorisation

A key project dependency is FCA authorisation progressing in line with the project plan. We learned during our review that POMS would consider becoming an Appointed Representative of Thistle in the event that FCA authorisation is delayed or unsuccessful. Whilst we were not asked to review this aspect we recommend that the POMS Board considers the viability of this option from a practical and reputational perspective, and documents a clear plan setting out the key risks and the controls required to manage those risks.

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Summary overview – Overall status by component

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Component	Summary commentary	Status as at 24/10/14	Status as at 21/11/14	Criticality
Governance	The POMS Board was not sufficiently engaged by the Project Titan team until the POMS Board meeting on 19 November 2014. During this meeting an action was taken to transfer the project into POMS. To achieve readiness for soft launch the POMS Board must now demonstrate its oversight of POMS is suitable, effective and appropriate for an FCA regulated entity.			Critical
Handover arrangements between Aon and POMS	The arrangements in place to manage the handover will require close oversight by the POMS Board to mitigate any adverse customer, regulatory and/or reputational impact, particularly where this could arise from a disagreement between Aon and AXA over regulatory responsibility for the ongoing management of Post Office policies.			Critical
Risk Management Framework	Key components of the risk management framework are in draft format and must be approved by the POMS Board before soft launch. Immediately post-launch the POMS Board must begin iterative testing in a live environment, to demonstrate that the framework is embedding effectively in practice, and is explicitly linked to POMS' developing risk appetite. To support this the POMS Board must ensure a suite of MI and Key Risk Indicators is developed that identifies current and emerging risks across the portfolio of POMS' activities, including outsourced activities.			Essential
Financial and regulatory reporting	Appropriate plans appear to be in place, but these cannot be robustly evidenced or demonstrated beyond statements made in interview. The POMS Board is considering proposals from external suppliers to deliver this critical function, but no supplier has been formally engaged.			Critical
Management Information	Detailed Management Information requirements are pending definition and development.			Essential
Outsourced arrangements	POMS' business model is critically reliant on outsourced arrangements. A number of key arrangements are yet to be finalised. Specifically soft launch cannot proceed without a signed agreement with the underwriter in place. This remains outstanding.			Critical
Approved Persons' responsibilities	The training materials POMS plans to use for its Approved Persons are not sufficient in isolation to fully prepare POMS' directors for the significant obligations they will be taking on. A plan is in place for POMS to enhance its Approved Persons' training regime.			Critical
Policies and procedures	A number of policies are incomplete, but are scheduled to be completed by the week commencing 24 November			Critical
Call centre compliance and ethical behaviours controls	The Project Team's description of the component's progress in interview and the significant volume of documentation provided suggest the work stream is on track. However, call centre compliance and readiness has not been fully tested or objectively reviewed. We noted a number of areas for immediate investigation in the Webhelp documentation provided.			Critical
Financial Promotions processes	The documented procedures for financial promotions are less detailed than we would expect and provide insufficient guidance in a number of key areas.			Essential
Customer journey – policy literature and customer communications	Policy documentation, process maps and Webhelp training material are in place. The policy booklet has not been completed, but a plan is in place for this to be delivered in time for soft launch.			Critical
Principal responsibilities between Bank of Ireland and POMS	The agreement governing arrangements between Bank of Ireland and POMS has been drafted, but has not been signed.			Critical

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POST OFFICE LTD BOARD

Reappointment of Non-Executive Directors

1. Purpose

The purpose of this paper is to:

1.1 Recommend to the Board that Virginia Holmes and Alasdair Marnoch be asked to renew their contracts when they are up for renewal in the new year; and

1.2 To request shareholder consent to re-appoint both non-executive directors to the Company.

2. Background

2.1 Virginia Holmes' term of office expires on 3 April 2015. Virginia acts as Chairman of the Pensions Sub Committee and Chairman of the Financial Services Committee.

2.2 Similarly, Alasdair Marnoch's term of office expires on 22 May 2015. Alasdair acts as Chairman of the Audit, Risk and Compliance Committee.

2.3 Shareholder consent will be required for both re-appointments to the Board, in line with the Company's Articles of Association.

3. Proposal

3.1 The Nominations Committee recommends to the Board that both directors be asked to renew their contracts for the non-executive positions and chairmanships of committees for 3 years from the dates of expiry of the current contracts.

4. Recommendations

The Board is asked to:

4.1 Recommend to the shareholder the appointment of Virginia Holmes and Alasdair Marnoch to renew their contracts in line with the Nominations Committee's proposal.

Nominations Committee
19 November 2014

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Post Office Limited – Strictly Confidential

POLB 14(10th)
POLB 14/127 -14/141

POST OFFICE LIMITED
(Company no. 2154540)
(the 'Company')

Minutes of a Board meeting held on 29 October 2014
at 148 Old Street, London EC1V 9HQ

Present:

Alice Perkins	Chairman
Neil McCausland	Non-Executive Director
Tim Franklin	Non-Executive Director
Virginia Holmes	Non-Executive Director
Alasdair Marnoch	Non-Executive Director
Richard Callard	Non-Executive Director
Paula Vennells	Chief Executive
Chris Day	Chief Financial Officer

In Attendance:

Alwen Lyons	Company Secretary
Mark Davies	Communications & Corporate Affairs Director (minutes POLB 14/128 - 129)
Neil Hayward	Group People Director (minutes POLB 14/128 - 129)
David Ryan	Business Transformation Director (minute POLB 14/128)
Nick Kennett	Director, Financial Services (minute POLB 14/133)
Paul Havenhand	General Manager POMS (minute POLB 14/133)
Kevin Gilliland	Network & Sales Director (minute POLB 14/134)
Lesley Sewell	Chief Information Officer (minute POLB 14/139)

POLB 14/127 **INTRODUCTION**

(a) A quorum being present, the Chairman opened the meeting.

POLB 14/128 **CEO'S REPORT**

(a) The CEO introduced her report and thanked the Board for convening for the additional Board call on the 21st October. The CEO focused on three key areas for discussion with the Board:

1. There was agreement that the Royal Mail Group (RMG) meeting taking place on the 30th October was vital and an opportunity to debate the changes in the market and each business's priorities. The Board recognised the changes required by Post Office would require a radical restructure for RMG, and asked the Business to ensure that if RMG was committed to these changes they understood the aggressive timeline that was required. The Board asked for an update after the RMG meeting.

ACTION:
CEO

2. The CEO emphasised that, whilst the Business remained committed to the existing plan, work was underway on an

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alternative plan (Plan B) which would include operating as an aggregator for other mails providers. It was acknowledged that this would need a renegotiation of the RMG MDA and that whilst the Business did not start from a strong negotiating position it needed to; protect sales volumes from RMG and not trigger a renegotiation from them; and reduce the complexity of the RMG product suits which would not switch easily to another provider.Plan B was also dependent on changes to the Network which would require Government support. The Board asked if the Business had the right resource working on Plan B. The CEO reported that she had approached Sue Barton, Strategy Director, currently on a sabbatical, but that she was unavailable until the New Year and that Martin Edwards was currently leading this work. Plan B was on the agenda for discussion at the November Board meeting.

3. The Board noted the improvement in the FS video mystery shopping to 80% compliance, and asked the FS sub committee to continue to monitor. The Board asked for an update on the mortgage sales and pipeline to give them comfort that the full year forecast was robust. The CEO explained that from next month Financial Services would be monitored as a key change programme in section 3 of her report.

ACTION: Nick Kennett

(b) The CEO updated the Board on Sparrow and an antagonistic conversation with James Arbuthnot MP about the Business' approach to the Mediation Scheme. She reiterated that the investigations were progressing well. The Business was refusing to progress all cases into mediation, although it was offering to meet and go through each case with the applicant. The Chairman offered to reconvene the Sparrow Board Sub Committee if required.

ACTION: Chris Aujard

POLB 14/129 **CEO RISK REPORT**

(a) The Board welcomed Neil Hayward, Group People Director, Mark Davies, Communications & Corporate Affairs Director and David Ryan, Business Transformation Director, to the meeting.

(b) The CEO introduced the risk paper and explained that the Business intended to have the necessary systems in place before the end of the financial year to enable it to comply with the UK Corporate Governance Code as it applies to risk management and report this in next year's Report & Accounts.

(c) The CEO explained that her report focussed on the areas highlighted in Sir Christopher Kelly's report on the Co-operative Bank, using his themes of Culture; Governance; Risk Management; and Capability. She believed that Capability was the biggest area of risk for the Business followed by the Culture of the organisation. In many areas these two themes were linked for example in risk management where the Business was increasing its capability at a senior level to lead the change in attitude and culture.

(d) The CEO reported that the recent PwC work to analyse the Business'

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ACTION: Chris Aujard

risk management had concluded that the Business capability was 'satisfactory' in steady state but 'inadequate' as the Business moved into transformation. The Board asked for a summary of the report to be circulated with the full report sent to those Board members who were interviewed.

(e) The CEO recognised that, as the Business accelerated the transformation and moved from design to implementation that the structure of the transformation team would need to change. She explained that the transformation office led by Alison Thompson would move to work for David Ryan, who would then lead the whole transformation agenda.

(f) The CEO assured the Board that the Business would only use consultants when absolutely necessary and that the CFO monitored this area. However, she recognised that especially in risk and change there was an urgency to get these areas in the position to be capable to deal with the transformation and this would need external resource.

(g) The CEO explained that enterprise risk, including the top 6+3 Business risks, would return to the January Board for discussion.

ACTION: Company Secretary

(h) The Board asked for updated forward agendas for Board and Sub Committee meetings

(i) The Board noted the Risk Report.

(j) David Ryan left the meeting.

POLB 14/130 **PEOPLE AND ENGAGEMENT UPDATE**

(a) Neil Hayward, Group People Director, introduced the update on the People and Engagement strategy, including the Plan for the next 12 – 18 months, changing the way that the Business works with the unions and the NFSP and stakeholder analysis and critical path.

(b) The Board recognised the challenge of people engagement during a period of significant transformation and cost reduction. Neil Hayward accepted that this would be challenging but reassured the Board that he had past experience of similar circumstances. He emphasised the need for a compelling narrative to help people understand why the changes were best for the organisation. Mark Davies explained that the tone of internal communications had already changed and people appreciated the honesty.

(c) Neil Hayward recognised that people needed to understand what the Business would be in 2020. He acknowledged that, as yet, the Business had not explained what a transformed and commercially sustainable Post Office would be like. He recognised that people would find the changes painful and agreed that the Business had to remain honest and consistent in its communication and paint a compelling picture of the future.

(d) The Board asked Neil Hayward if he was constrained by the resource in his team and which areas he would like to accelerate work on. He

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explained that he kept the resource in the Industrial Relations Team under review, but acknowledged that his two areas of concern were refreshing the Senior Leadership Team which took a lot of his and Fay Healey's personal time and senior leadership development.

ACTION: Neil Hayward

(e) The Board asked for an update at the end of the Financial Year to review the roadmap for the next 12-18 months and the senior leadership training and development.

(f) Neil Hayward explained that Wave 1 of the new organisational design would be presented to the Nominations Committee on the 10th November. He reported that the Business has also recognised that retention may become an issue for specialist areas and that his team was considering a very small number of people who may require retention payments.

ACTION: Chris Aujard

(g) The CEO emphasised the need to focus more on subpostmasters but stressed the need to keep them as agents and not employees. The Board were concerned that these definitions should not be blurred. The CEO agreed and promised a note to the Board from the General Counsel (GC) to give them comfort.

(h) The Board discussed and supported the proposed changes to collective bargaining and was reassured by the Business' plans. Neil Hayward stressed the need to get down to the right level of representation for the Business with a formula that reduces in line with headcount.

(i) The Board considered the detail of possible simultaneous CWU and NFSP disputes and the likely reaction of stakeholders. Mark Davies explained the worst case scenario and although he did not underestimate how difficult it would be, believed the Business had the capability to handle both the operational and media battles. The Board asked for assurance that the Business could manage the operational consequences of a strike. This issue would be raised with Kevin Gilliland, Network Director later in the meeting.

(j) The CEO assured the Board that the plans were already in place for Christmas and that any NFSP dispute was likely to be after the Christmas period. Neil Hayward explained that the next contentious point of negotiation with the NFSP was likely to be the Memorandum of Understanding and grant agreement, the principles and price of which he was still discussing.

(k) The Board asked Richard Callard for his opinion of the Minister's likely response to any disputes. He explained that the Minister had already been briefed regarding the CWU Supply Chain dispute and considered it an operational issue in which she should not get involved, although she was supportive of the Business and understood the possible need to use compulsory redundancy. He suggested that the relationship with the NFSP was more complicated. The Minister understood the need to manage Network Transformation within the current funding envelope, which would be impossible if additional compensation was paid to subpostmasters for network extension. He could not promise how the Minister would respond but

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promised the Shareholder team, ShEx and the Treasury support.

(l) The Board asked Richard Callard to ensure that any Ministerial briefing made clear the financial consequences of failure. The CEO explained that she had a meeting with the Minister in the next two weeks at which she would be able to explain the position.

ACTION: Mark Davies

(m) The Board asked the Business to refresh the stakeholder plan, and produce a high level heat map/stakeholder grid to keep the Board updated. The Chairman recognised that the Board does not have a meeting in December but asked the CEO to keep the Board informed and if necessary call an emergency Board meeting

(n) The Board noted the update on People and Engagement, and supported the proposals presented.

(o) Neil Hayward and Mark Davies left the meeting.

POLB 14/131 **FINANCIAL PERFORMANCE UPDATE**

(a) The CFO presented a financial performance update for September 2014.

(b) He explained that his report would cover the changes in forecast since period 5; the full year outlook including key dependencies and assumptions for H2 performance; a year on year comparison of H1 performance; and external messaging for the interim statements.

(c) The CFO full year forecast for income had worsened from the £890m in period 5 flagged by the CFO at the last Board meeting, down to £880m, £45m behind budget and £13m up on the previous year. This was driven by two areas where the CFO had taken a more prudent approach to the forecast.

(d) The Mails income had been reduced to include a more realistic return for the ebay and mails coaching initiatives, but still contained growth for the Christmas campaign which the Business supported.

(e) In addition Government Services net income had been reduced by £10m to recognise the liability for deceased customers. The CFO explained that the Business continued to hope it can offset this liability with the income for 'ring-fenced' customers but this had not proved possible to date so it was necessary to recognise the liability at P6. The Board discussed the possible pricing true-up issues and supported the CFO's prudent approach in recognising the liability whilst not including any benefit for the undercharging for ring-fenced customers.

(f) The CEO assured the Board that the inaccuracies caused by the DWP and Business systems had not led to any customer detriment.

(g) It was noted that Government Services income was down 10% on last year at the half year and likely to be similar at full year.

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(h) The Board were concerned about the effect of the new telephony contract. The CFO explained that a new plan was now in place which had taken down the expected customer numbers as well as the average revenue per user. He considered that there was still £3m risk in the telephony numbers despite a price rise in January which should improve the position by £2m. The telephony contract was due to come to the Risk & Compliance Committee and then the ARC for a deep dive in the New Year.

ACTION: Chris Aujard/ Alasdair Marnoch

(i) The CFO explained that significant challenge had gone into scrutinising the income numbers through a formal review process and that the Commercial and FS teams were signed up to delivering the new forecast.

(j) The CFO reported the changes to the cost forecast and the current gap of £15m against the adjusted target of £60m required to protect the original EBITDAS. He still believed the Business would get near to the £60m target if one off savings such as releasing the bonus accrual were included. However, the forecast had been reduced to include the £45m he was certain the Business could deliver.

(k) He stressed the importance of finding sustainable savings in the year and was hopeful the Business would get to near its adjusted target of £53m, which was required to underpin the £100m cumulative sustainable saving required by the end of 2015/16.

(l) The CFO concluded that, taking into consideration the changes to income and costs, he had reduced his EBITDAS forecast to £85m, including a £5m contingency. He explained that the likely year on year improvement in EBITDAS (after allowing for material one off adjustments) was circa £20m, which would deliver a projected EBITDAS of circa minus £75m this year and a likely trajectory to breakeven in 2 to 3 years' time, rather than 1 year indicated in the 2013 funding request.

(m) The Board was concerned by the status of the Business scorecard and asked specifically about the Easy to do business with (ETDBW) decline and whether this was a reflection on cost cutting. The CFO explained that very few front line jobs had been cut, but accepted that there seemed to be a disparity between ETDBW and the customer research undertaken after network transformation. The CEO explained that the two measures were very different and promised to return to the Board for a discussion on ETDBW.

ACTION: Martin George

POLB 14/132 **INTERIM REPORT AND CONDENSED FINANCIAL STATEMENTS FOR 2014-15**

(a) Mark Davies joined the meeting.

(b) The Board reviewed the Company's draft interim report for the 2014-15 half year.

(c) The Board agreed that the statement should explain the journey the

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Business was on and the turnaround taking place. It should show that the Business is doing the right things and has taken some pain in the first half of the year but that the rate of improvement is getting better. It needs to explain the cost story, including necessary investment, and why the Business needs to go harder and faster.

ACTION: Mark Davies

(d) Mark Davies agreed to provide a revised draft for the Chairman and CEO.

(e) Mark Davies left the meeting

POLB 14/133

PROJECT TITAN/POST OFFICE MANAGEMENT SERVICES LIMITED (POMS)

(a) The Board welcomed Nick Kennett, Financial Services Director, and Paul Havenhand, General Manager POMS, to the meeting and received an update from the POMS Board on the insurance transformation programme.

(b) Virginia Holmes, Chairman of the FS Sub Committee explained that the FS sub committee had not had an opportunity to review the work, although she had been called by Nick Kennett and the General Counsel (GC) to take her through the paper with which she was very comfortable. The area she had concentrated on had been the contingency around the Thistle risk.

(c) Nick Kennett reported that the setting up of POMS was broadly on track with Directors appointed, bank accounts opened and auditors in place. He explained that the preliminary assurance paper from Grant Thornton had identified two red areas of risk:

1. that the POMS Board needed to be seen to be managing the Business with a clear structure for ownership and separate roles and responsibilities from Post Office.
2. that effective run off arrangements between AXA and AON had still to be agreed.

ACTION: Chris Aujard

Nick Kennett explained that the GC would provide a risk paper for the November Board including the conclusions from Grant Thornton, to enable the decision on commencement of trading.

(d) The Board discussed the two decisions needed to enable POMS to trade and the contingencies in place. If (based on the Grant Thornton advice) the GC could not give assurance that POMS was ready to trade, the Post Office would contract with Collinsons in the interim under an introducer arrangement as it did with Aon currently. This would be at an additional cost of £100k to set up and £80k a month.

(e) If the FCA did not give approval to POMS but the Board agreed commencement of trading the Business would use Thistle as an intermediary at a cost of £70k to set up and £100k a month to run.

(f) The Board were given assurance that there would be no customer detriment if the Business needed to use either of these contingencies or with the setting up of POMS.

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(g) The Board also received a request to approve the POMS three year business plan and discussed the growth assumptions. Paul Havenhand explained the potential in the aggregator channel and the minimal risk of packaged accounts.

(h) The Board:

- Noted the update from the POMS Board and that a final decision regarding POMS' commencement of trading would be tabled at the November Board meeting for approval.
- Approved the POMS three year plan.
- Authorised the POMS Board to execute lead contracts with underwriters that meet the risk threshold of a Standard & Poors (or equivalent) rating of at least A-.
- Noted that the selected underwriter to act as the underwriter lead was Great Lakes (a Munich Re subsidiary) with Collinsons managing claims and Solid providing additional capacity (c. 20%) for non-standard policies.

(i) The Board discussed Project Hawk and Nick Kennett reported that he had written to the Bank of Ireland (BoI) IRRELEVANT and had received their IRRELEVANT He explained that the Business would now revert to the use of an Independent Expert (IE) to opine on the IRRELEVANT The critical date for signing the Hawk contract was 31st March 2015. The Board asked Nick Kennett to ensure the terms of reference for the IE specified the necessary timeline for the work and that progress would be made in agreeing the shortlist, whilst he was on leave. The Board asked Chris Day, as Chairman of POMS, to ensure this happened.

ACTION: Nick Kennett/ Chris Day

(j) Nick Kennett and Paul Havenhand left the meeting.

POLB 14/134 **NETWORK UPDATE**

(a) The Board welcomed Kevin Gilliland, Network & Sales Director, to the meeting and received an update on Network Transformation, performance of the new models and progress on Crown Transformation.

(b) The Board were encouraged by the progress and thanked Kevin Gilliland for the strong Network Transformation performance.

(c) The Board discussed Crown Transformation and the likely profit and loss run rate at year end. Kevin Gilliland explained that the Business may miss the breakeven target by 6 months but that the Crown Transformation was still a remarkable turnaround. The Board agreed and was sympathetic to the position and discussed the additional actions which could be taken. The Board asked the Business to ensure that all legitimate actions were delivered including recognition of the additional profit in the franchise network. Kevin Gilliland was asked to provide a narrative to explain the transformation delivered in the Crown network to be used to support the year end run rate.

ACTION: CFO/Kevin Gilliland

(d) The Chairman explained the earlier Board discussion, POLB 14/13 (i), and asked Kevin Gilliland to reiterate his contingency plans in the

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event of Supply Chain industrial action, specifically to give the Board comfort that the Business could manage both discontinuous and continuous action with little customer detriment.

(e) Kevin Gilliland explained the process of pre-funding the network and the use of the rapid deployment force (250 trained managers) to manage any difficult parts of the country.

(f) He believed that continuous action was highly unlikely but in this event the network would be pre-funded with the 3000 more remote branches getting 5-10 weeks cash. He remained confident that the Business could manage any action with little disruption to customer service. The Board asked the Business to be ready to handle the PR around any closed branches.

(g) The Board affirmed its support for the approach to the Supply Chain negotiations and any subsequent industrial action.

(h) The Board noted the Network update.

(i) Kevin Gilliland left the meeting.

POLB 14/135 **BOARD EFFECTIVENESS REVIEW**

ACTION: Chairman

(a) The Board accepted the Chairman's offer to undertake an internal Board effectiveness review in the New Year. Alasdair Marnoch, Chairman of the ARC, asked for clarification of Directors' responsibilities specifically pertaining to POMS. Virginia Holmes explained that as Post Office did not hold a banking licence the NEDs responsibilities would not change. The Non-Executive Chairman of POMS would be considered the responsible person.

POLB 14/136 **MINUTES OF PREVIOUS MEETINGS AND MATTERS ARISING**

(a) The minutes of the Board meetings held on 25 September 2014 were approved for signature by the Chairman.

POLB 14/137 **COMMITTEE MEETING MINUTES FOR NOTING**

(a) The Board noted the minutes of:

- the Audit, Risk and Compliance Committee held by correspondence on 16 September 2014; and
- the Financial Services Sub-Committee meeting held on 16 September 2014.

POLB 14/138 **STATUS REPORT**

(a) The Status Report, showing matters outstanding from previous Board meetings, was noted.

(b) The Board noted the update on the Facilities Management and Grapevine contract awards.

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POLB 14/139 **END USER COMPUTING (EUC) CONTRACT AWARD**

(a) The Board approved the award of the EUC contract to Computacenter and authorised the CFO to execute the relevant contracts.

POLB 14/140 **ITEMS FOR NOTING**

(a) The Board noted the Cyber Security update.

(b) The Board noted the Significant Litigation report.

(c) The Board noted the Health & Safety report.

(d) The Board noted the Report on Sealings and resolved that the affixing of the Common Seal of the Company to the documents set out against items numbered 1123 to 1230 inclusive in the seal register was hereby confirmed.

POLB 14/141 **DATES OF NEXT MEETINGS**

(a) It was noted that the next Board meeting would be held on 26 November 2014.

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POLARC14 (4th)
14/31 - 14/36

POST OFFICE LIMITED
(Company no. 2154540)
(the **Company**)

Minutes of a meeting of the AUDIT, RISK AND COMPLIANCE SUB-COMMITTEE held on 21 October 2014 by conference call.

Present:	
Alasdair Marnoch	Chairman of Committee
Neil McCausland	Senior Independent Director
Tim Franklin	Non-Executive Director

In attendance:	
Alwen Lyons	Company Secretary
Chris Aujard	General Counsel (GC)
Chris Day	CFO
David Mason	Head of Risk Governance
Malcolm Zack	Head of Internal Audit
Gavin Lambert	Chief of Staff

POLARC 14/31 **INTRODUCTION**

A quorum being present, the Chairman of the Committee opened the meeting and welcomed all those present.

POLARC 14/32 **MINUTES OF THE LAST MEETINGS AND MATTERS ARISING**

(a) The Committee approved the minutes of the meetings held on 15 May 2014 and 16 September 2014 for signature by the Chairman of the Committee.

(b) The Committee noted the actions list dated 17 October 2014.

POLARC 14/33 **RISK APPETITE STATEMENTS**

(a) The GC introduced the risk appetite statement and explained that the Business intended to have the necessary systems in place before the end of the financial year to enable it to comply with the UK Code of Corporate Governance as it applies to risk management and report this in next year's Report & Accounts. The enterprise wide risk management system incorporating the risk appetite would be used to understand and highlight risks as the Business moved in business transformation.

(b) The GC noted the importance of providing metrics and tolerance ranges for each element of the risk appetite statement as a practical guide for the Business, and recognising that the statement provided was only the first draft, asked the committee members for their input.

(c) The ARC was encouraged by the developing risk management framework, but still had concerns about the time taken to get all the components established in Post Office.

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(d) Specifically around the risk appetite statement the business was asked to:

1. Focus on more actionable statements with clear metrics behind each element.
2. Ensure the overall framework was established before populating each individual dimension
3. Reconsider the ratings used as 'Receptive' was considered too neutral for the 4th rating, and 'cautious' and 'minimal' were too similar to enable clear differentiation .

(e) The Committee members considered the risk categories in the statement and suggested 'customer', 'commercial partners' and 'change' could also warrant consideration as separate categories. They proposed that the high level general statement of appetite needed to be supplemented by more detail.

(f) The Committee gave the following specific feedback for each area:

Markets: They suggested that 'markets' should be differentiated to show more detail for the different markets in which the Business operates as well as any proposed new markets. The Business should be keen to take on risk in the markets in which it is established (either 'receptive' or 'hungry') but it should be much more cautious when entering new markets. They agreed that the Business should focus on their existing markets rather than committing investment to diversify. Lower profits would be acceptable to maintain revenue in mature markets, but not to the extent that this would be loss-making. The Committee understood why the Business would be neutral about Government contracts, given the recent history, but still felt enthusiastic about this market if conditions were right.

Financial: The Committee agreed that the sub categories were too narrow and that the Business should consider wider financial risk. It suggested highlighting appetite for asset/liability management; cost reduction; efficiency; and anything which might drive profitability through financial constraints or measures. It was thought that this was an area where the Business could be much more specific. All three members were 'hungry' to be free of subsidies.

Legal/regulatory: There was general support for this area although simpler language would be helpful when describing high profile matters.

People: The Committee recommended inverting the statements. For example 'hungry' for getting the right people with the right skills. They also asked the Business to consider including a specific reference to unions within the people section of the risk appetite.

Technology: There was general support for this area but the Committee though that as a business incorporating financial services, the risk appetite for any data inaccuracies should be 'averse'.

Operations: no comments.

Stakeholder: Impressed by statement around the potential to 'lose engagement of a key stakeholder' and considered this one of the best statements in the paper.

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(g) Corporate affairs: they acknowledged the importance of this dimension over the coming months and had no concerns with the wording.

ACTION: DM/GC

ACTION: GC

(h) The Committee agreed that the draft appetite statement was a good starting point and directionally correct. The Chairman suggested that the Business take the specific feedback from the Committee, but to focus on a detailed redraft of the Market dimension for presentation at the November ARC meeting.

(i) The Committee agreed to bring the risk appetite statement to the January Post Office Board Meeting.

(j) The GC reminded the Committee that PwC were undertaking a review of the risk framework and business change management capability. Their report would be tabled at the Business' Risk and Compliance Committee in November. The change management assurance would be incorporated into the Business Transformation work for the November Board.

GC also reported that the Business would review its top risks again in January.

POLARC 14/34

INTERNAL AUDIT UPDATE

(a) The Committee received an update on the Post Office Internal Audit activity and key outcomes from June to September 2014.

(b) Malcolm Zack reported that there were no major issues with the implementation of the new finance system which went live in September. The remaining written assurance report on IT General Controls would be provided at the final programme board. He stated that the programme aimed to formally close down in the next week, although internal audit would continue to monitor.

(c) Malcolm Zack reported that the audit of Benefits Realisation had found no serious issues, but had highlighted a number of process points specifically around tracking financial and non-financial benefits through to conducting PIRs. The CFO agreed that the report raised valid concerns around the culture of the business and accountability. He assured the committee that the Business was working to tag benefits to programmes and ensuring the right people were accountable

ACTION: GC

(d) Malcolm Zack reported on the audit of the Business Continuity planning and noted that the overall plan was not yet complete. He explained that work was on-going and needed the business continuity manager to brief the ExCo and SLT, so that they were aware of the key steps to take in an emergency. The business aimed to address this by the end of the calendar year. The GC would bring an updated on the major incident/disaster recovery timetable to the ARC in January. It was agreed that the ARC would continue to monitor.

(e) The Committee noted the outcomes of the recent audits and reviews and the current and upcoming work.

(f) The Committee noted the amended Internal Audit 2014/15 plan.

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ACTION: MZ

(g) The Committee noted the status of audit recommendations and actions and requested that where actions were rebased that the new timeline be included to show a more accurate RAG status.

ACTION: GC

(h) The Committee asked if internal audit were considering a value for money audit of Network Transformation. Malcolm Zack stated that this was not currently in the plan. The CFO assured the Committee that he was in on-going discussion with the NAO to ascertain if they were likely to audit BiS, which they are not, and how the Business could best evidence value for money.

(i) The Committee was given assurance that the Internal Audit resource with the addition of PwC support was adequate providing the financial level of PwC support was maintained as per the co-source arrangement.

(j) David Mason and Malcolm Zack left the meeting.

ACTION: GC

(k) The GC explained that Malcolm Zack had handed in his notice and would be leaving the Business on the 31st December. It was agreed that the possible interim replacement be invited to attend the next ARC. It was agreed that when a new candidate is identified that they would meet the Chairman of the ARC as part of the interview process.

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DATE OF NEXT MEETING

The date of the next meeting is 10 November 2014.

POLARC 14/36

CLOSE

There being no further business, the meeting was declared closed.

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PC 14/41-14/43

POST OFFICE LIMITED
(the 'Company')

PENSIONS SUB-COMMITTEE

Minutes of a meeting of the Pensions Sub-Committee of the Board held at 148 Old Street, London EC1V 9HQ on 28 October 2014

Present:	Neil Hayward (NH)	(in the Chair)
	Virginia Holmes (VH)	
	Chris Day (CD)	
	Richard Callard (RC)	
In Attendance:	Keith Murdoch (KM)	Head of Reward and Pensions
	Natasha Wilson (NW)	HR Consultant
	Harpreet Singh (HS)	Pensions Manager
	Alwen Lyons	Company Secretary
	Larissa Wilson	Secretariat
	Phil Daniels (PD)	Senior Client Manager, Mazars

PC 14/41 OPENING OF MEETING

A quorum being present, RC and CD nominated NH to act as Chair of the meeting in VH's absence.

PC 14/42 DEFINED CONTRIBUTION PENSION SCHEME

The Committee welcomed PD to the meeting and received a recommendation from Mazars that the Company should appoint Friends Life as the Group Personal Pension Plan provider from 1 April 2015.

PD explained the tender process behind Mazars' recommendation, which had involved inviting ten providers to participate in the market tender exercise, nine of which responded (AEGON did not respond) and were assessed against the following criteria:

- Quality (Business Requirements), accounting for 80 per cent of total weighting:
  - Implementation
  - Administration/Information Security and Data Protection
  - Communications
  - Investments
  - Technology
- Pricing, accounting for 20 per cent of total weighting:
  - Range of funds offered
  - Default options
  - Individual funds

The shortlisted providers (Friends Life, Legal & General and Zurich) were then interviewed by representatives from Mazars Employee Benefits and Post Office, including union representation.

PD reported that both Friends Life and Zurich had very good responses at tender and interview stages. One of the factors which differentiated the Friends Life tender had been the quality of the proposed member communications, including access to their pension details from their PC,

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tablet and mobile phone. Both companies highlighted the extensive library of pensions information they had online. Friends Life also demonstrated a strong commitment to the Company offering a dedicated helpline, retirement options and pre-retirement seminars at no additional cost. Friends Life had made it clear that Post Office would be a very valuable client to them and that they would be willing to work with the Business and the unions to help member engagement.

Friends Life had offered a good range of funds at competitive prices, if 90-95% of employees opted for the default option this would be provided at a 40% reduction compared with RMDCP charges. The Committee discussed the tender process and were satisfied with how it had been conducted and that it followed the spirit of the Public procurement process in the fact that it was conducted openly, fairly and transparently.

ACTION: PD/HS

The Committee requested that the providers' updated scores after the interview stage be added to the Mazars recommendation paper.

VH joined the meeting.

The Committee discussed the importance of market commitment and the financial strength of Friends Life and Zurich. The Committee considered the current financial strength ratings from Standard & Poors (S&P) and Moody's, with Friends Life's S&P rating of A- and Moody's rating of A3 being lower than Zurich's S&P rating of AA- and Moody's rating of Aa3. The Committee requested clarity over the significance of these ratings from Mazars.

ACTION: PD/HS

The Committee discussed the solvency ratios for both providers. PD reported that both had adequate solvency ratios under Solvency I, with Friends Life at 193% and Zurich Group at 270%. VH challenged the use of Solvency I ratios and asked Mazars to provide Solvency II ratios as these new requirements would soon be more appropriate and were more stringent.

ACTION: PD/HS

The Committee considered the funds available and the investment performance of Friends Life's default fund. PD reported that the fund had only a short track record as it had been set up fairly recently in readiness for auto-enrolment, its return to date had been at 9.1% against a bench mark of 7.6%, with volatility at 7% against a benchmark of 12%. PD agreed to provide comparable statistics for Zurich and statistics for the consolidation phase of both providers' default solutions.

ACTION: PD/HS

RC questioned whether Friends Life would offer value for employees as, aside from the default option, some of the options were more expensive compared to other providers. HS and NH assured RC that it was highly likely that the majority of employees would opt for the default option, which had a very competitive annual management charge (AMC) of 0.27%. It was also explained that the other funds presented may not necessarily be selected, although funds with higher AMCs may provide higher returns. PD explained that members would have the opportunity to change their options as often as they wanted and emphasised the significant increase in fund options that both Friends Life and Zurich offered in comparison to the current scheme.

VH raised questions regarding how Post Office's employees would hold

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their interests in the Friends Life funds and the transfer process from the existing RMDCP scheme into the new scheme. PD clarified that Post Office would be part of the pooled fund and that employees would be allocated units of this fund. Under the bulk transfer process members would select their options before a designated cut-off date and be transferred at a designated transfer date. The funds would be valued as at the cut-off date for selection and Friends Life would pre-purchase at 95% with the result that out-of-market risk would apply to only 5%, with most transfers taking place within 24 hours to reduce out-of-market risk. Friends Life was also willing to transfer members on an individual basis, although these transfers would not be pre-purchased. VH emphasised the importance of agreeing a minimum bulk size with Friends Life. The Committee also considered the importance of proper communication with employees and NW assured the Committee that the Business would be working with the unions to ensure that people understood the process.

ACTION: PD/HS

VH requested clarification on the status of any outstanding Resolution issues that Friends Life had with the FCA and PRA.

The Committee supported Mazars' recommendation to appoint Friends Life as the Group Personal Pension Plan provider from 1 April 2015 in principle and authorised the Business to proceed to discuss the recommendation with the unions.

The Committee agreed to recommend the proposal to the Post Office Executive Committee after the Business's conversations with the unions and the receipt of the information requested during the meeting.

It was noted that any decision to appoint a defined contribution scheme provider would be subject to a consultation of the Post Office members of the RMDCP scheme.

PC 14/43 **CLOSE**

There being no further business, the meeting was declared closed.

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POST OFFICE LIMITED BOARD
Status Report

No.	REFERENCE	ACTION	BY WHOM	STATUS
		1. Strategy		
1a	May 2014 POLB 14/65(f)	Draft necessary amendments to the Remuneration Committee Terms of Reference to enable it to make recommendations to the Post Office Board on appointments to the POMs Board.	**Company Secretary**	To be tabled at Remuneration Committee on 10th November
1b	May 2014 POLB 14/69(e)	Deliver a separate and accurate P&L account and balance sheet for the Supply Chain Business.	**CFO**	In progress, subject to management review in October Update - The new Finance system design provides the functionality to provide robust channel P&L's, including one for the Supply Chain business. We are currently testing the Channel P&L's as part of the implementation, and should be in a position to report these for the end of November.
1c	September 2014 POLB 14/114(a)	Provide clarification on the impact of the Common Digital Platform on the Horizon system and any possible cost savings.	**Martin George**	To be included in the digital noting paper being prepared for the January Board
1d	October 2014 POLB 14/128(a)	Provide an update to the Board after the RMG meeting on 30 October.	**CEO**	Update: 2/11 - Paula sent an update on RMG by email.
		2. Win in Mails		
2a	September 2014 POLB 14/106l	Provide a paper for the Board, ahead of the Chairman/CEO with RMG in October, highlighting the 3 or 4 issues which needed to be resolved and showing these issues and opportunities from the perspective of both Businesses.	**Martin George**	Paula sent an update on RMG by email.
2b	September 2014 POLB 14/106(h)	Encourage the NFSP to take up the invitation for a sub postmaster to join the network extension development	**Kevin Gilliland**	Work in progress. (Next meeting with NFSP is 24th Oct). UPDATE: 18/11 -

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		team.		Current position from NFSP is that they will not engage in detailed discussions relating to Network extension until the MOU is signed. Therefore further consideration of a spmr being placed at Bishopsgate will not be made (by either party) until the detailed discussions on NE take place.
2c	September 2014 POLB 14/106(i)	Prepare a 3 year operating plan to confirm the detail of the network extension work.	**CFO**	November Board UPDATE – This will be picked up through the Business Transformation roadmap which is coming to the November Board, this will include network development/extension.
		3. Financial Services		
3a	September 2014 14/105(e)	The Business to identify the critical leading indicators for monitoring changes in customer behaviour and circulate to the Board.	**Nick Kennett**	This will be included as part of the Three Year Plan being presented to the November Board.
3b	September 2014 14/105(f)	Present the results of the six month trial where Post Office FS colleagues used Mains branches as their base.	**Nick Kennett**	May Board
3c	September 2014 14/105(h)	Prepare a BoI paper outlining the Post Office and BoI positions on initiatives through to 2023, and the effect of the relationship on short term performance and longer term strategy.	**Nick Kennett**	Paper going to the November Board
3d	September 2014 14/105(i)	Analyse on present to the Board on whether the Business should focus more on the innovation of the pre-paid debit account rather than the current account as on the effective hook for customers	**Nick Kennett**	Update 19/11: Will revert to the FSSC in the New Year.
3e	October 2014 POLB 14/128(a)	Provide an update on mortgage sales and pipeline to give the Board comfort that the full year forecast was robust.	**Nick Kennett**	Update 21/11: SEE APPENDIX 1 BELOW

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3f	October 2014 POLB 14/133(c)	Provide a risk paper for the November Board, including the conclusions from Grant Thornton, to enable the decision on the commencement of trading of POMS.	**General Counsel**	November Board
3g	October 2014 POLB 14/133(i)	Ensure that the terms of reference for the independent expert engaged as part of Project Hawk specified the necessary timeline for the work and that progress would be made on agreeing the shortlist whilst NK was on leave.	**Nick Kennett/Chris Day**	Update 19/11: Timelines specified and work progressed
		4. Business Transformation		
4a	September 2014 POLB 14/104(c)	The Board to receive the full Business Transformation proposal at the November meeting, which would include the stakeholder and IR plan.	**David Ryan/Neil Hayward**	November Board
		5. People and Engagement		
5a	October 2014 POLB 14/130(e)	Provide an update at the end of the financial year to review the People and Engagement roadmap for the next 12 -18 months and the senior leadership training and development.	**Neil Hayward**	March 2015
5b	October 2014 POLB 14/130(g)	Provide a note on the relationship between Post Office and subpostmasters.	**General Counsel**	Work is underway and a note will be circulated to the Board when it becomes available
5c	October 2014 POLB 14/130(m)	Refresh the stakeholder plan and produce a high level heat map/stakeholder grid to keep the Board updated.	**Mark Davies**	UPDATE 18/11: My recommendation is that we include the heat map/grid in the CEO report to the Board every month and circulate to ExCo each week, with a monthly stakeholder slot at ExCo.
		6. Risk		
6a	July 2014 POLB 14/90(h)	The ARC to review the Risk Management framework.	**General Counsel**	Draft went to October ARC. Final version to be discussed at the January ARC and Board.
6b	October 2014 POLB 14/129(d)	Provide a summary of PwC's report on the Business' risk management and circulate to the Board. Send the full report to those Board members who were	**General Counsel**	Summary attached. Full version circulated to the interviewed Board members.

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		interviewed.		
		7. Miscellaneous		
7a	July 2014 POLB 14/101(c)	Arrange a cyber-security guest speaker to attend a future Board meeting.	**Company Secretary / Richard Callard**	January Board
7b	July 2014 POLB 14/101(d)	A Board meeting to be held at the Post Office Design Lab at the Southbank University.	**Company Secretary/Martin George**	In the New Year
7c	September 2014 POLB 14/109(e)	The Business to work with ShEx to update the Minister on the Post Office position regarding the investigations, the Scheme and Second Sight as part of Sparrow.	**Belinda Crowe/General Counsel/Richard Callard**	The CEO wrote to the Minister on 14 October
7d	October 2014 POLB 14/129(d)	Provide forward agendas for Board and Sub-Committee meetings.	**Company Secretary**	In progress. Board schedule attached.
7e	October 2014 POLB 14/131(h)	Telephony contract to go to the Risk and Compliance Committee and then the ARC for a deep dive in the New Year.	**Chris Day/Alasdair Marnoch**	To January ARC
7f	October 2014 POLB 14/131(m)	Return to the Board to discuss ETDBW.	**Martin George**	Update 20/11: We are returning to ExCo before Christmas to discuss how we measure customer feedback and then act on the insights. We will brief the Board early in the New Year.
7g	October 2014 POLB 14/134(c)	Provide a narrative to explain the transformation delivered to the Crown network to be used to support the year end run rate.	**CFO/Kevin Gilliland**	
7h	October 2014 POLB 14/135(a)	Undertake an internal Board effectiveness review in the New Year.	**Chairman**	

Appendix1 – Mortgage Update (Action 3e)

At the end of October across all channels we had completed £1,102m against a target of £973m YTD. Combining the income generated from these completions with the back book income we receive, as at end of October we were approximately 113% of target.

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However, since August our applications pipeline has reduced significantly, initially as a result of having to withdraw products due to BOI's processing problems, but more recently due to a non-seasonal slowdown in the housing market which has reduced market volumes. Consequently, we have seen our pipeline of business reduce significantly to £342m, of which approximately £290m will complete by the end of the financial year.

To address this we have introduced a more tactical approach to pricing which has seen a more frequent refresh of products. This has enabled us to maintain a continuous best buy presence over the last few weeks which has resulted in a 20% increase in 'web leads' (November over October) for our Mortgage Specialists which is driving an increase in activity levels. With the direct channel we have a strong focus on aggregators and affiliates linked to our price competitiveness. Our product range also includes a strong re-mortgage proposition in-addition to the movers and first time buyers ranges. We will continue with this approach into the new year when mortgages will also benefit from a strong focus in our Q4 campaign.

We are confident that the more tactical approach to managing products / rates and continued marketing focus will help us to drive applications and grow the pipeline to ensure we achieve our income budget of £7.3m by the financial year end.

Nick Kennett
21 Nov 2014

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MANAGEMENT IN CONFIDENCE

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Post Office Limited Risk Management Capability

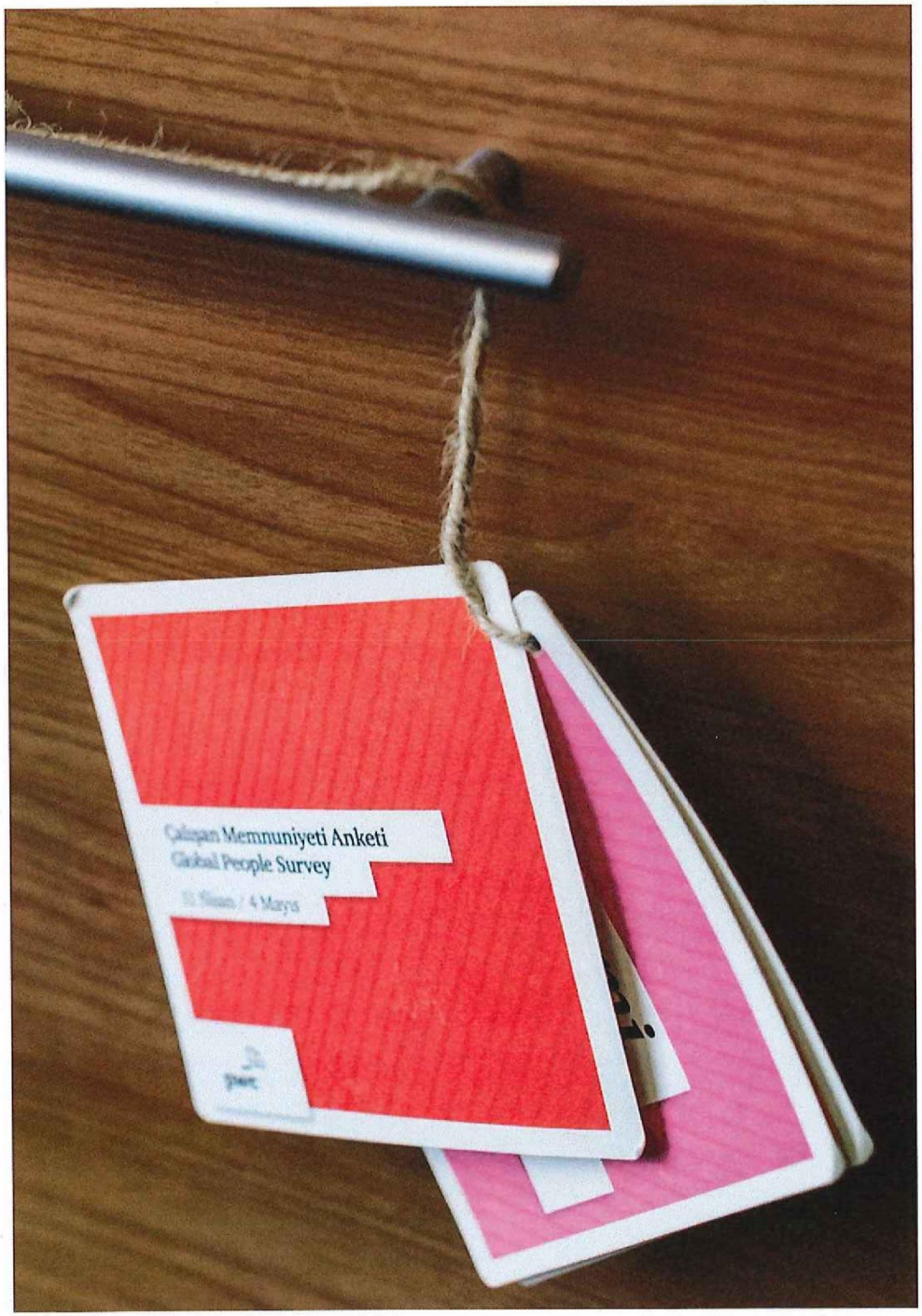
FINAL REPORT

November 2014

IRRELEVANT

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MANAGEMENT IN CONFIDENCE

Executive Summary

Scope

PwC was asked to carry out an independent review to look at the extent to which Post Office Ltd (POL) has the appropriate risk assurance arrangements in place across both the organisation and its change portfolio.

We were asked to do this in the context of POL having a good historic track record of delivering individual programmes of change – however it is now facing unprecedented levels of change as it transitions from the public sector to the commercial sector over the next few years.

We carried out a strategic diagnostic comprising of 35 interviews, attendance at key governance meetings including the Transformation Committee and Risk & Compliance Committee, undertook a document review and close working with POL colleagues.

We were asked to present our findings in a practical, forward looking way to assist POL with direction on where and how to improve.

Our terms of reference and details of interviews are included in Appendix C and D.

Context, Constraints and Key Assumptions

POL combines a strong brand and a passion for safeguarding it's future, with the very real challenges of putting its operation on a much stronger commercially and financially viable footing. This is not an organisation in crisis but an organisation in transition.

At the time of writing this report, although we were able to discuss in general terms the extent of change facing the organisation (from short term turnaround to get costs under control to medium term transformation plans to deliver on the 2020 Strategy), we have not been privy to detail around the 'Business Transformation' Programme. We have therefore made the simple but reasonable assumption that POL face a significant amount of change in the name of 'Business Transformation'.

POL is still operating in the context of being public sector, by legacy if not by destination, with the additional complexity of running two quite different businesses – mail and financial services and with a network that is increasingly integrated with the retail sector (e.g. through the supermarkets).

In agreement with POL, we have therefore benchmarked POL against what we would expect to see in place to manage the risks associated with a commercial, FTSE 250 organisation.

Recognising that POL is only just starting its transition journey, we didn't expect POL to meet all of the standards expected of a FTSE 250 company. However, we believe this benchmark has been useful in highlighting a number of short term recommendations that POL needs to action as well as setting out some longer terms considerations if POL aims to mature their approach to the management of risk.

Approach and What You Told Us

PwC used its Risk Maturity Framework to assess POL in terms of where it is now and where it aims to be in terms of delivering on its 2020 Strategy. Our maturity assessment rates organisations on a scale of 1 to 5.

The next page provides a range of direct quotes from our interviews – these are some of the things you told us – and we provide them as a powerful illustration to support our subsequent analysis as set out in the rest of this report.

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MANAGEMENT IN CONFIDENCE

Executive Summary

The following statements were taken from interviews with stakeholders. They reflect some of the opinions that have informed our Findings.

Board

"We don't want to manage risks by lists"

"The Post Office have a strong brand but there is a lack of understanding of our risks.

"The word risk seems to have negative connotations to people and they do not understand the benefits and the value that sound risk management can bring"

ExCo/ Programme Sponsors/ Programme Directors

"There is a need for a formal process to define risk appetite if only to ensure everyone is on the same page"

"We need a central function who can provide support, direction and 'challenge'....helping to shape how risks are reported and managed through ensuring the central understanding of risk"

POL00149638

Executive Summary

The Maturity Journey

All organisations evolve and mature over time. POL is a new organisation, having recently separated from RMG, and to that extent it is still working to establish a clear identity and purpose. It is not surprising therefore to find that it is taking time for POL to develop the appropriate checks and balances needed to manage risk or indeed the change lifecycle and assurance gates to ensure the effective management of more complex change. Historically POL has a good track record of delivering individual programmes and has managed both 'run' the business while 'changing' the business.

POL has not been complacent and there is a good level of awareness of the need to mature as POL ups its ambitions, with a number of steps already taken to appoint key personnel, review and strengthen governance structures and processes. This review is an example of that awareness and intention to build out and mature over time.

In many ways, in steady state, the current arrangements would broadly suffice – although we have been able to make a number of, hopefully helpful, suggestions to target and expedite further improvement. However, given the POL change mandate, which we have assumed to be fairly radical, the delta between where POL is and where it needs to be is even bigger. This report establishes the 'as is' baseline and makes recommendations which POL need to action in order to accelerate the improvements to risk management needed to support business transformation to deliver the 2020 Strategy and associated transformation plans.

The Strategic Areas Where Focus is Required

Based on our assessment there are a number of inter-related areas where POL needs to apply strategic focus to accelerate it's level of maturity.

1) **Culture and behaviours:** If POL is still finding its identity, it is not surprising to find that POL is still working to establish a clear culture and norms. There isn't yet a clear 'POL way' of doing things. Investment of time, particularly with the senior leaders in the organisation is needed to work this through, if they are to provide a strong and consistent narrative throughout the POL transformation journey.
2) **Governance:** Although the Board and committee structure is fit for purpose, there is a lack of clarity around roles and responsibilities which undermines the ability for the governance structures to effectively operate. For example, we found little evidence of colleagues holding one another to account.
3) **Working in a complex transformation environment:** Requires a stable culture, agreed norms, clear accountabilities and indeed a governance structure that supports decision making. It also requires senior leaders to do the right thing, work in a matrix structure and deliver the strategic agenda over and above their functional responsibilities. Addressing the two previous points would reduce the risks posed in relation to business transformation.
4) **Equipped for Business Transformation:** POL has the systems and processes in place to manage small scale change and risk within individual functions. It needs to equip itself with the vision, culture, processes, people and systems to deal with complexity and stress the organisation will undertake as part of Business Transformation. As part of our recommendations we have identified the need for POL to:
    - Better define its risk appetite and the common framework as to how it will manage risk across the organisation
    - Equip itself with the right tools and processes including a common change language, the improvement in Management Information and upskilling of its change capability with the experience of undertaking transformational change

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Board and Sub Committee Dates

Last Updated : 20/11/2014

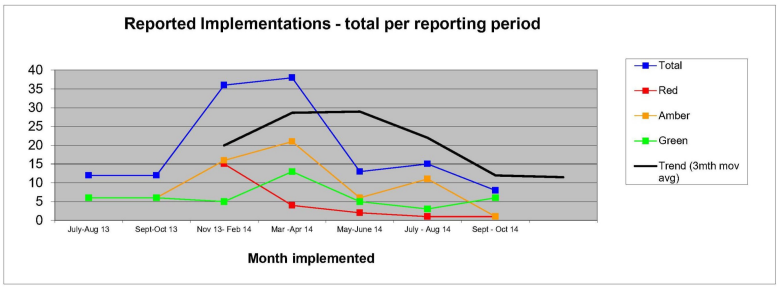
2014	POL Board	ARC	RemCo	NomCo	FS Committee	Pensions Committee	POAC
November	26th 09.00hrs to 17.00hrs	10th 12.00hrs to 14.00hrs	10th 14.15hrs to 15.45hrs	10th 15.45hrs to 17.15hrs			12th 09.15hrs to 14.00hrs
December					3rd 13.30 hrs to 15.30hrs	3rd 10.00hrs tp 12.00hrs	
2015	**POL Board**	**ARC**	**RemCo**	**NomCo**	**FS Committee**	**Pensions Committee**	**POAC**
January	28th 09.00hrs to 17.00hrs	12th 10.30hrs to 12.30hrs					
February			25th 09.30hrs to 11.00hrs	25th 11.00hrs to 12.30hrs			
March	25th 09.00hrs to 17.00hrs				3rd 15.00hrs to 17.00hrs	11th 10.00hrs to 12.00hrs	19th 10.00hrs to 14.00hrs
April							
May	21st 09.00hrs to 17.00hrs	27th 12.00hrs to 14.00hrs	13th 13.00hrs to 14.30hrs	13th 14.30hrs to 16.00hrs			
June	17th & 18th (Timings TBA)				3rd 10.00hrs to 12.00hrs	26th 10.00hrs to 12.00hrs	
July	15th 09.00hrs to 17.00hrs		8th 10.00hrs to 11.30hrs	8th 11.30hrs to 13.00hrs			1st 10.00hrs to 14.00hrs
August							
September	22nd 09.00hrs to 17.00hrs	16th (via Phone) 16.00hrs to 17.00hrs			9th 10.00hrs to 12.00hrs		
October	28th 09.00hrs to 17.00hrs	15th 12.00hrs to 14.00hrs				1st 10.00hrs to 12.00hrs	
November	25th 09.00hrs to 17.00hrs	10th 12.00hrs to 14.00hrs	3rd 10.00hrs to 11.30hrs	3rd 11.30hrs to 13.00hrs			4th 10.00hrs to 14.00hrs
December					9th 10.00hrs to 12.00hrs	3rd 10.00hrs to 12.00hrs	

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Status as at October 31st 2014

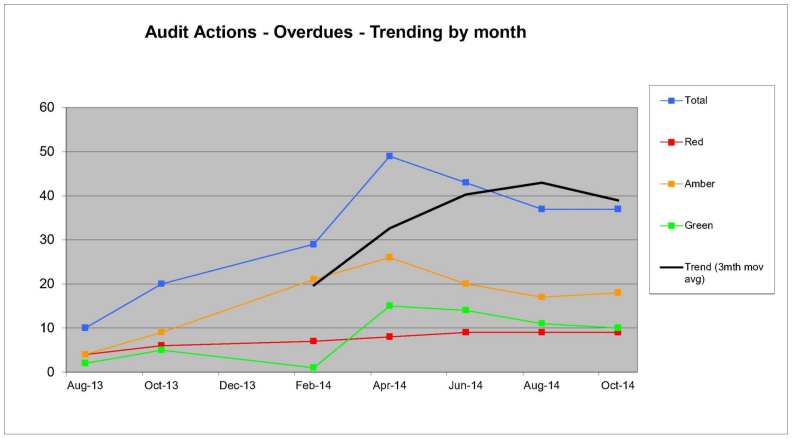
	Total	Red	Amber	Green	
Total actions outstanding bfwd as at 31st August 2014	37	9	17	11	
Implemented by Mgt - Sept- October 2014	(8)	(1)	(1)	(6)	
Actions added (audits and advisory)	25	3	13	9	
Superceeded/amended	3		1	2	
Carried Forward as at October 31st	57	11	30	16	
Analysis of Carried forward					
Overdue - yet to start	0				
Overdue - Work in progress	37	9	18	10	
Not yet due	20	2	12	6	new
	57	11	30	16	

Trends



Reported Implementations	Total	Red	Amber	Green
July-Aug 13	12		6	6
Sept-Oct 13	12		6	6
Nov 13- Feb 14	36	15	16	5
Mar -Apr 14	38	4	21	13
May-June 14	13	2	6	5
July - Aug 14	15	1	11	3
Sept - Oct 14	8	1	1	6
Cumulative	134	23	67	44

Implementation down in period, mainly because of newer items that are not yet due and known revised target dates for IT actions.



Overdue as at	Total	Red	Amber	Green
31-Aug-13	10	4	4	2
31-Oct-13	20	6	9	5
20-Feb-14	29	7	21	1
30-Apr-14	49	8	26	15
30-Jun-14	43	9	20	14
31-Aug-14	37	9	17	11
31-Oct-14	37	9	18	10

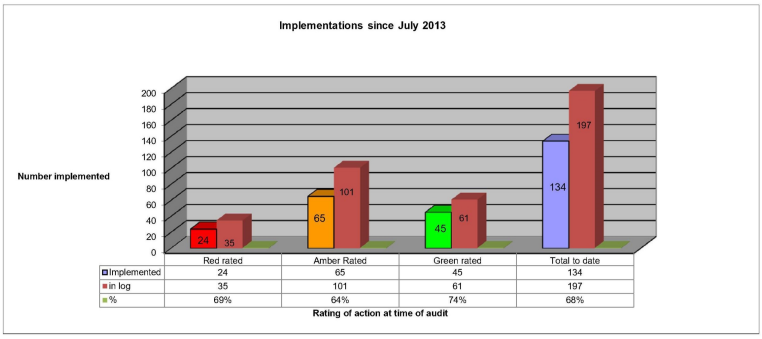
IMPORTANT NOTE - IT ACTIONS HAVE BEEN REBASED WITH NEW TARGET DATES LATE 2014 and into 2015 to reflect changes in expected implementations of towers

The IA recommendations log still retains the ORIGINAL target date so that the business is fully aware it is still aware of the risks identified in the audit and these are still in place.

Rebasing of dates for some IT actions due to later than planned tower implementations. Some items however in Identity and Access Management and software licensing are just overdue with delays in management action or changes in ownership.

The IT Governance and Controls manager position vacated in July 2014 has not been filled. Responsibilties passed to a senior member of the CIO team.

Implementations in period are within Benefits Realistion, Business Continuity and minor issues in HR



Implementations achieved (from June 2013)

	Implemented	Total in log	%
Red rated	24	35	69%
Amber Rated	65	101	64%
Green rated	45	61	74%
Total to date	134	197	68%

IA logs the total actions agreed with the business and tracks implementations since the final transition from Royal Mail IA in June 2013

The total implementation rate was above 70% during the summer, however there is a slight dip below ongoing target level due to the lower implementation rates in September and the addition of audit actions from recent audits. A number of these however (20) are not yet due. So implementation rate should recover above target line after the new year.

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November 2014

POST OFFICE LIMITED MATTERS – DISPUTE RESOLUTION
PRIVILEGED AND CONFIDENTIAL – CLAIMS OVER £500K OR THOSE OF A SENSITIVE NATURE

PART (A) – CIVIL LITIGATION

FILE NAME	CASE HOLDER	BUSINESS UNIT & CONTACT	DESCRIPTION	STATUS	XSP
Horizon claims (aka "Project Sparrow")	POL/RW	Belinda Crowe / Angela van den Bogerd	POL has received various claims from subpostmasters (SPMs) alleging defects in the Horizon system and POL's internal processes. These allegations were initially made in 5 claims brought through solicitors Shoosmiths. Similar allegations have been made by the "Justice for Subpostmasters Alliance" (JFSA) and advanced through SPMs' MPs. Following discussions with James Arbuthnot MP and JFSA, independent investigator Second Sight Support Services Ltd (Second Sight) was appointed in July 2012 to carry out a review into these allegations. On 08.07.13, Second Sight published a Report finding shortcomings in POL's internal training and support to SPMs on the Horizon system, but no systemic problems with Horizon itself. Following the Second Sight Report, on 27.08.13 POL launched a Mediation Scheme (Scheme) aimed at resolving individual complaints made about Horizon.	This matter will be the subject of a separate update to ExCo. The Scheme received 150 applications, which are being progressed under the direction of a Working Group comprising retired Court of Appeal Judge Sir Anthony Hooper (as Chair), POL, Second Sight, and JFSA. 127 cases are still being progressed through the Scheme or are being scheduled for mediation. Mediations have been held for the first 4 applications. A further 8 mediations are currently being scheduled. The POL project team continue to handle the applications in line with the Board's direction to take a firmer position, informed by its legal position and tighter control over timescales and costs. To date, no claim has been made against POL in the civil courts, and no appeal has been made against any conviction in the criminal courts, following Second Sight's Report.	Bond Dickinson

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Employment	POL/NM	Colin Stretch	**Legal Privilege**	**Legal Privilege**	Eversheds

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				Legal Privilege	
Employment	POL/NM	Colin Stretch	**Legal Privilege**	**Legal Privilege**	Weightmans

PART (B) – CRIMINAL LITIGATION

PROSECUTION CASES

There are number of cases which could have been prosecuted (e.g. those with full and frank admissions to theft /fraud), but prosecutions were not commenced to avoid adverse judicial comment.
Several cases have also been terminated while POL obtains an independent expert report on the Horizon branch accounting system (see below).
There are currently 14 cases which are being kept under review as to whether a prosecution (supported by an expert report) can be commenced.

EXPERT REPORT

New experts from Imperial College London have prepared a scope of work on which formal instructions and a protocol for requesting and receiving information will be based.
Appropriate individual confidentiality agreements will be prepared for both for the experts and POL employees involved in preparing the report.
Meetings to progress the report are taking place between the experts, POL and Fujitsu in September and October 2014.

PROSECUTION POLICY

Former First Senior Treasury Counsel Brian Altman QC has drafted a proposed prosecution policy for POL.
Comments from POL stakeholders will now be sent to Brian Altman for review.

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POST OFFICE LTD BOARD

Health & Safety Report

1. Purpose

The purpose of this paper is to:

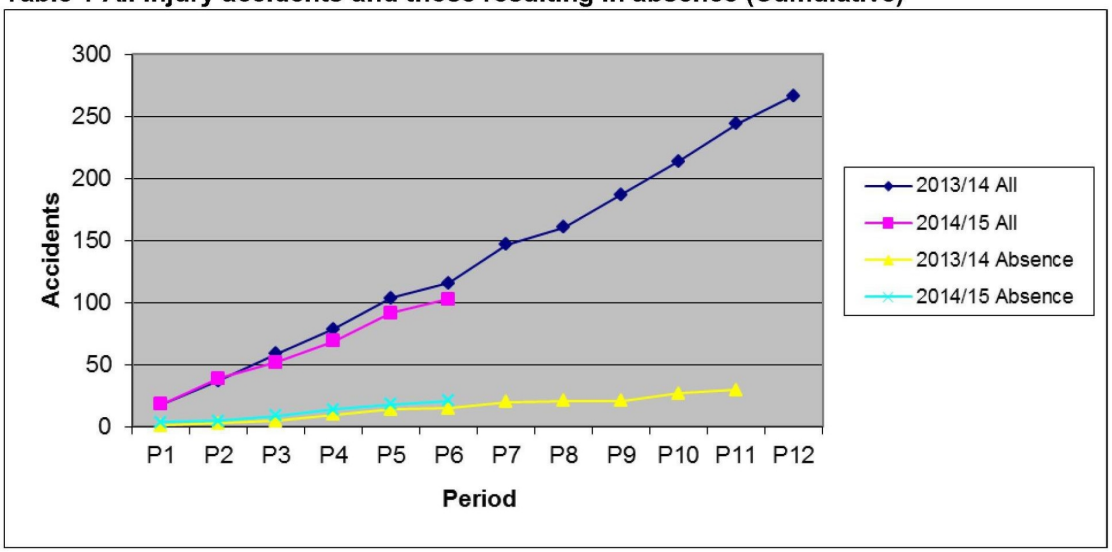
1.1 Provide an update on safety performance.
1.2 Outline risk reduction activities.

2. Current Situation

2.1 The majority of accidents fall into three main categories lifting and handling, stepping and striking and outdoor falls. These are higher frequency events with, in the majority, relatively low severity. The lower frequency types of incident can carry the potential for very high impact, for example, assaults and road traffic collisions.

2.2 Performance during the first six months of 2014/15 indicates that despite the slight adverse performance in absence accidents and days lost there is no current cause for concern that further reductions by year end are achievable and in line with the 5% year on year reduction target. The reduction of all injury accident incidents is currently ahead of target.

Table 1 All Injury accidents and those resulting in absence (Cumulative)



2.3 Personal injury compensation claims have fallen significantly in line with the reduction in accidents that result in sick absence. Claims involving members of the public have also reduced. Comparison with a similar retail organisation indicates that the Post Office claim rate is significantly lower in both public and employer's liability and of those claims the 'denial' or 'defence' rate is significantly more successful. The insurance year runs from October to September. (Table 2 below refers)

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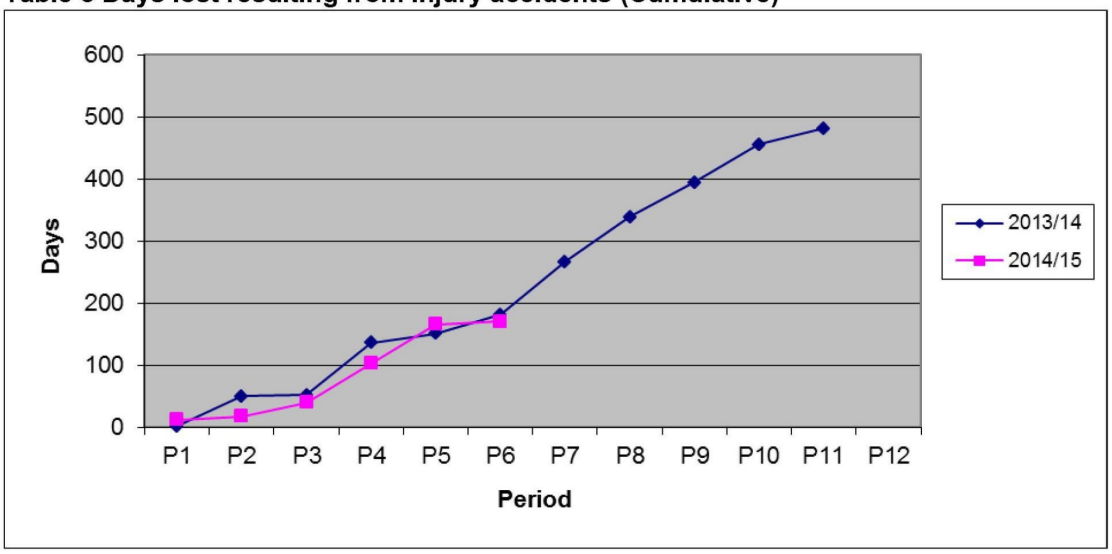
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Table 2 Employers Liability and Public Liability claims since October 2012 – extract from insurers report.

UW Year	Policy Class	Claim Count	Total Paid	Recoveries	Open Reserves	Gross Incurred	Net Incurred
2012	Employers' Liability	7	£8,200	£0	£37,946	£46,146	£46,146
	General Liability	17	£33,961	£0	£106,577	£140,539	£140,539
	Total	24	£42,161	£0	£144,524	£186,685	£186,685
2013	Employers' Liability	2	£360	£0	£20,034	£20,394	£20,394
	General Liability	10	£10,352	£0	£32,900	£43,252	£43,252
	Total	12	£10,712	£0	£52,934	£63,646	£63,646
Total	Total	36	£52,873	£0	£197,458	£250,331	£250,331

2.4 The number of days lost due to accidents is marginally adverse against target however it is anticipated that the year on year reduction target of 5% will be achieved. (Table 3 below refers)

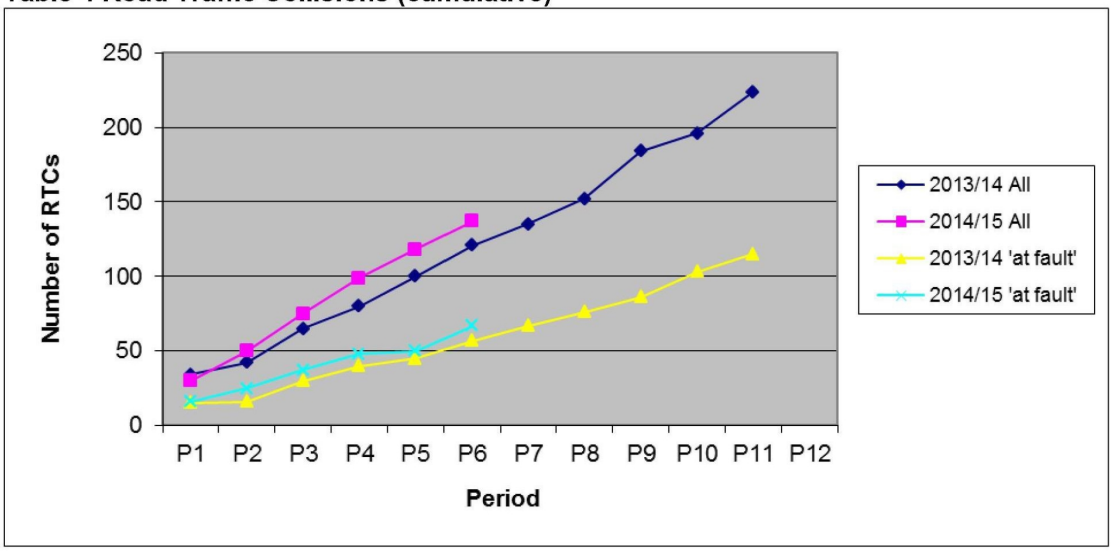
Table 3 Days lost resulting from injury accidents (Cumulative)



2.5 The total number of road traffic collisions (RTCs) for the first 6 months is up 16 on last year. While this is of concern it is believed that there continues to be a more robust approach to the reporting of incidents, irrespective of severity, and what appears to be an increase in minor damage incidents e.g. broken mirrors and minor scrapes The number of incidents where the Post Office driver is 'at fault' is showing an increase of 10 compared to last year. (Table 4 refers) Road risk reduction opportunities continue to be the subject of analysis at the Road Risk Forum with a view to identifying improvement activities in addition to those already in place. (3.1 below) Reversing incidents are currently a cause for concern and will be the subject of additional attention. Injuries as a result of road traffic collisions are extremely infrequent. Road traffic collisions account for less than 3% of the overall number of injury accidents, however they have the potential for high impact in terms of injury and loss. Currently the majority of incidents involve low speed – less than 25mph.

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Table 4 Road Traffic Collisions (cumulative)



2.6 Robberies on Post Office Cash and Valuables in Transit (CViT) crews are down three on last year from 20 to 17 for the past 6 months. Physical injuries during robberies, of which there have been 5, 1 more than last year for the same period, remain relatively minor in severity. The level of use of firearms is down 2 on last year with 3 of the 17 robberies enabled by the presence and/or threat of use of fire arms and on no occasions were the firearms discharged. Support for those affected by robberies is provided by trained trauma supporters and professional support resources available through the occupational health service provision. Risk reduction activities are identified at 3.2. (Appendix 1 – Significant Incidents refers)

2.7 Robberies and attempted robberies on the Post Office network, for the past 6 months, are up 1 on last year to 44 of which 59% were successful. Injuries sustained during robberies are down from 9 to 5. Robberies take place predominantly at sub post offices leaving Crown branches largely unaffected although Wandsworth Crown Branch suffered a robbery on 1st October 2014. Supporting activities have been introduced to continue to mitigate the robbery risk and are identified at 3.2. (Appendix 1 – Significant Incidents refers).

3. Activities

3.1 Road Risk

Current activities to mitigate road risk are:

- Road risk forum in place to scope and develop road risk reduction initiatives and activities supported by the risk management division of our insurers
- Analysis and deployment of interventions for reversing incidents to mitigate the increased incidence rates, including yard assessments and technical accident reduction interventions on new vehicles e.g. Reversing aids to reduce accidents
- Analysis and evaluation of data including risk profiling to identify drivers who need additional support and to determine further generic accident reduction interventions
- Safe driver of the year award to encourage and reward responsible driving
- Weekly case conferences to ensure consistent approach to accident investigation, follow up activity and sharing of good practice

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- Programme of driving and road risk communications to raise awareness of current and emerging risks

3.2 Robbery/Burglary Risk

Current activities to mitigate robbery and burglary risk are:

- Active liaison activities with the police to understand 'at risk' areas and to deploy surveillance teams
- Increased use of 'advertising' on vehicles of new deterrent technologies e.g. DNA taggant – a solution that contains a unique identifier that is released automatically in the event of a robbery, spraying those involved and enabling identification of the individuals involved in the robberies
- Trialling new point of transfer arrangements to reduce exposure at Post Office counters - the majority of robberies take place at the point of transfer which in Post Office's is the counter where there is ready public access. The new arrangements allow for the cross pavement protection box to be emptied / filled in a secure location.
- Significant reduction in opportunities for duress type robberies linked to the introduction of single person vehicles – single person vehicles eliminate the opportunities for Supply Chain employee duress type incidents which historically have been the most violent and likely to involve injury.

3.3 Health and Wellbeing

Healthcare interventions:

- Second programme of visits to Crown branches, Supply Chain units and Admin offices to offer health checks using equipment that provides a wide range of indicators on physical wellbeing. The anonymised data is used to develop future health and wellbeing campaigns and target interventions.
- The programme of visits is supported by an online 'Wellbeing Zone' health check tool as a 'self- help' option
- Ongoing campaign of communications to promote a range of different wellbeing issues
- Wellbeing events to promote general health, exercise and dietary initiatives

3.4 Safety

The Post Office occupational health and safety management system (OHSMS) is certified by external auditors to the standards required by British Standard OHSAS 18001.

3.5 Asbestos Management

Transfer of the ownership of asbestos management following separation has led to a programme of actions to ensure that up-to-date surveys are available, defined responsibilities post-split are clear and that an asbestos management 'action plan' is in place to ensure that these issues can be managed effectively and in line with legislation. Legal Services have been engaged to advise on responsibilities, particularly in relation to the agency network, and to ensure arrangements for on-going management of asbestos are robust and risks mitigated.

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3.6 Network Transformation (NT) - Safety

Discussions continue with legal services in respect of responsibilities in relation to appropriate health and safety support for the agency network. Considerable time and effort has been put into defining, obtaining legal sign-off for and incrementally implementing procedures to support and improve the Health and Safety processes in relation to network transformation and associated works.

4. Residual Risks

4.1 Driving activities have the potential for high impact/loss and therefore remain as a significant residual risk. However, the actions identified in 3.1 above are aimed at mitigating that risk and improving performance.

5. Recommendation

The Board is asked to:

5.1 Note the overall safety performance
5.2 Note the risk reduction activities.
5.3 Note the residual risks

Neil Hayward
November 2014

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Appendix 1

Significant Incidents (Period 6)				
Crowns and Network				
Location	**Loss**	**Circumstances**	**Physical Injuries**	**Any further details**
Gala Park SPSO, 8 Balmoral Place, Galashiels, TD1 1JE	£2,870	IRRELEVANT		
Royton MSPO, 60 Rochdale Road, Royton, OL2 6QQ	£12,891			
Dumers Lane SPSO, 263 Dumers Lane, Manchester, M26 2GN	£4,792			
Supply Chain				
Location	**Loss**	**Circumstances**	**Physical Injuries**	**Any further details**
Cheetham Hill SPSO, 6 King Edward Building, Bury Old Road, Manchester, M7 4QJ	£26,000	IRRELEVANT	None	
Ravenhead SPSO, 117-120 Ravenhill Road, Belfast, BT6 8DR	£21,000		None	

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POST OFFICE LIMITED BOARD

Sealings 22 October 2014 – 18 November 2014 inclusive

Register of Sealings

The Directors are invited to consider the seal register and approve the affixing of the Common Seal of the Company to the documents set out against items numbered 1231 to 1240 inclusive in the seal register.

"The Directors resolve that the affixing of the Common Seal of the Company to the documents set out against items numbered 1231 to 1240 inclusive in the seal register is hereby confirmed."

Alwen Lyons
Company Secretary
18 November 2014

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POST OFFICE LIMITED

Register of Sealings

Date
18/11/2014

Company Number
2154540

Seal Number / File Ref.	Date of Sealing	Date of Authority	Description of Document	Persons Attesting To Document	Destination of Document
1231	29/10/2014	29/10/2014	TR1 relating to Title number LN102706 between Post Office Limited and Ajay Thakarshi Kukadia	Alwen Lyons	Jean Reynolds
1232	29/10/2014	29/10/2014	TR1 relating to Title number NGL898655 between Post Office Limited and Ajay Thakarshi Kukadia	Alwen Lyons	Jean Reynolds
1233	29/10/2014	29/10/2014	TR1 relating to Title number NGL899365 between Post Office Limited and Ajay Thakarshi Kukadia	Alwen Lyons	Jean Reynolds
1234	29/10/2014	29/10/2014	TR1 relating to Title number NGL901217 between Post Office Limited and Ajay Thakarshi Kukadia	Alwen Lyons	Jean Reynolds
1235	30/10/2014	30/10/2014	Deed of surrender of lease at Ground Floor, Leamington Spa FPO, 1 Priory Terrace, Leamington Spa, CV31 1AA between Post Office Limited and Royal Mail Estates Limited	Piero D'Agostino	Jean Reynolds
1236	05/11/2014	05/11/2014	Counterpart/Retrospective Licence for Alterations relating to Part Ground Floor Premises, Bristol & West House, 39-41 Boutport Street, Barnstaple, Devon, EX31 1SA between the Cooperative Bank plc and Post Office Limited	Alwen Lyons	Jean Reynolds
1237	07/11/2014	07/11/2014	Letter licence to occupy 9-10 Kings Street, Carmarthen, Dyfed 11 November 2014 between 10.30am - 11.30am between Sian Elizabeth O'Leary, John Heddwyn Davies and Post Office Limited	Piero D'Agostino	Jean Reynolds
1238	10/11/2014	10/11/2014	Deed of variation of the collaboration agreement between Post Office Limited, WH Smith High Street Limited and WH Smith Travel Holdings Limited	Piero D'Agostino	Sabrina Jethwa
1239	14/11/2014	14/11/2014	Lease of Ground Floor Room TX-G-02, Town Hall Extension, St Peter's Square in the City of Manchester between the Council of the City of Manchester and Post Office	Piero D'Agostino	Jean Reynolds
1240	17/11/2014	17/11/2014	Agreement for sale of a property at 13-14 High Street, Southampton, SO14 2DF between Post Office Limited and Harkalm Estates Limited	Alwen Lyons	Jean Reynolds

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POST OFFICE LTD BOARD

UPDATE ON STATE AID PROCESS

1. Purpose

The purpose of this paper is to request the Board to note the latest events in relation to the on-going State aid application process for Post Office's 2015-18 Government funding package.

2. Background

Under EU State aid rules, Government must obtain State aid clearance from the European Commission ("**Commission**") prior to transferring any funding to Post Office. Therefore, it is imperative that Government obtains State aid clearance for the 2015-18 funding agreement prior to 1 April 2015, the date on which Post Office is due to receive its 2015 annual payment.

Since early 2014, Post Office has assisted Government in obtaining State aid clearance for the 2015-18 funding agreement, in particular by preparing submissions to the Commission case team that is managing the State aid application process.

Post Office's Restrictions Policy has become an issue of relevance to the State aid application process. The Restrictions Policy prevents sub-postmasters from offering certain services that can be provided by Post Office ("**Restricted Services**") in a private capacity, unless Post Office has granted a waiver.

The European Commission's previous State aid clearance decision of Post Office's funding for the 2012-15 period contains the below misleading statement about the Restrictions Policy ("**2012 Statement**"):

> "*The contracts that Post Office has with the sub-postmasters are such that other network operators can sign contracts with any sub-postmaster to deliver services which are not offered by Post Office. As a consequence, were Post Office to lose any contract to an alternative provider, this provider can use Post Office's network of sub-postmasters to provide this service.*"

Specifically, the second sentence of the 2012 Statement is inaccurate unless 'any contract' is interpreted as a contract for a non-Restricted Service or a contract that is covered by a waiver.

Since 2012, we understand that PayPoint has complained to the Commission that the Restrictions Policy is not operated as per the 2012 Statement and / or is otherwise unfair.

On foot of its contacts with PayPoint, during a meeting in June 2014, the Commission case team expressed concerns about the Restrictions Policy to Post Office and Government. In doing so, it pointed to concessions from exclusivity arrangements in relation to post offices that have been granted by BPost and La Poste in recent State aid clearance procedures.

In response to these concerns, in August 2014 Government (with Post Office's approval) offered to relax the Restrictions Policy in a limited way. In short, subject to certain caveats, we offered to grant competitor access to a post office in any case where a competing provider of Government-funded services (Government services, utility bill payment services, basic banking services, and postal services) shows that there is no retail premises except a post office in a postcode district. Out of 2,812 postcode districts in the UK, we calculated that there are around

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395 districts with less than 5 retail premises. On this basis, it appears that a competitor should not be able to satisfy the terms of the August 2014 offer except in a low number of rural areas.

In October 2014, Government (with Post Office's approval) responded to a concern by the Commission case team that the August 2014 offer included certain 'subjective' caveats. This concern was addressed without changing the fundamental terms and scope of the offer.

3. Current Situation

On 13 November 2014, the Commission case team issued what have been described as its final questions that, if resolved, will enable it to start preparing a State aid clearance decision for approval by the Commission and eventual publication. On Tuesday 18 November, Post Office and Government attended an update call with the Commission case team to discuss their questions.

Set out in sections 4 to 6 below is a summary of the questions that are noteworthy and our proposed responses.

4. Request for Change to Limited Offer to Relax the Restrictions Policy

The Commission case team has requested the deletion of a caveat that was included in the latest October 2014 offer and is shown in strike-through below. The caveat was most clearly relevant to bill payment contracts. It allowed Post Office to refuse access to a competitor that has met the geographic criteria where Post Office already offers the same service on behalf of the same client (eg, where Post Office and Payzone both hold contracts with SSE).

> *Upon receipt of a written request from a provider of a service that competes with a Product SGEI, which demonstrates that no contact point other than a Post Office Branch can be used by customers of the relevant service in a particular postcode district, Post Office shall grant access to its network to that provider. Access will be granted by Post Office permitting one Post Office Branch identified by it in that postcode district to fulfil a contract to provide the relevant service for the applicant.*
>
> *Such access will be granted provided that it would not: (i) materially impede Post Office s ability to provide the SGEIs entrusted to it, in particular in accordance with the Entrustment Letter and the strategy and targets as set out in the Funding Agreement (e.g. in respect of service quality or where access would lead to capacity constraints for Post Office); (ii) be prejudicial or detrimental to Post Office's brand or positioning (e.g. where access would be in conflict with communities' or customers' expectations of Post Office Branches); or (iii) be inconsistent with the regulatory obligations of Post Office or its commercial partners. ~~Access would only be granted where Post Office does not hold a contract with the applicant's upstream supplier (if applicable) to deliver the same relevant service throughout Post Office's network.~~*

4.2 Options Considered

We have considered the options of (i) accepting the request, and (ii) refusing the request. Each of these decisions would be communicated to Government as it (and not Post Office) is the addressee of any communications with the Commission case team.

4.3 Proposal

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We are minded to accept the request to delete the above caveat, for the following reasons:

- The amended wording appears a successful outcome for Post Office, taking into account that (i) the Commission case team indicated in June 2014 that it would seek radical changes to the Restrictions Policy, and (ii) the above wording is significantly narrower than the 2012 Statement, which covered all post offices and all lost contracts.

- It is not clear that Post Office would find itself capable of invoking the above caveat in many (of the few anticipated) competitor application cases. For example, it appears reasonable to assume that any client and / or competitor of Post Office would be less interested in delivering a service through rural post offices in circumstances where Post Office is doing this (unless the competitor already has a terminal installed in the relevant rural post office).

While the amended wording appears acceptable and low risk to the commercial interests of Post Office, its implementation (following its publication in the State aid decision in around April 2015) will involve challenges for Post Office. Chief among these will be:

- ensuring that Post Office remains capable of complying with its exclusivity obligations to Royal Mail and BOI (by relying on the caveats at (i) to (iii) above);

- handling communications with subpostmasters and retail partners who may see this new commitment by Post Office as an opportunity to challenge the Restrictions Policy; and

- managing the administrative burden involved in setting up and managing a proper application procedure to be used by competitors seeking access to rural branches on the basis of this new commitment by Post Office.

5. Question on Newspaper Article Regarding the Restrictions Policy

The Commission case team has raised the following question by reference to the attached news article:

> *"We have received concerns by competitors that the State subsidized network transformation of Post Office is performed at the expense of competitors (evidenced for example in the newspaper Article in the attachment). In order to address these serious concerns, we would like to receive your authorities confirmation and reassurance that the network transformation does not involve the exclusion of competitors from part of their network."*

5.2 Options Being Considered

It appears necessary for the Government to provide assurance to the Commission case team that Network Transformation does not involve any conduct by POL that is unjustified or inappropriate. While achieving this objective, as of 19 November 2014, we are considering the options of either:

- Suggesting the Government explain to the Commission why Post Office does not foreclose competitors from their networks, but noting that new sub-postmasters do agree to comply with the Restrictions Policy which means that they cannot provide Restricted Services on behalf of competitors; or

- Suggesting the Government simply provide the assurances that the Commission case team has requested without reference to the Restrictions Policy.

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6. Public Consultation on Need for Government Funding of Post Office

The Commission case team is seeking a commitment from Government to go out to public consultation on the public need for the Government-funded services provided by Post Office before making a new State aid application for funding post-2018. The most recent consultation of this type was done by NERA in 2009 and the report is available on Ofcom's website.

7. Recommendations

The Board is asked to note the update and actions set out above.

Chris Aujard
19 November 2014