

OFFICIAL SENSITIVE  
COMMERCIAL

**To:** Permanent Secretary  
**From:** Siv Rajeswaran, Manager, UKGI  
**SCS clearing:** Roshana Arasaratnam, Executive Director, UKGI  
**Date:** 24 October 2022

**Meeting Brief: Lisa Harrington Call, NED Post Office Limited**

**Date, time and location of meeting:** 27 October 2022, 2pm, MS Teams

**Meeting attendees:**

- Lisa Harrington, Chair of Remuneration Committee, Post Office Limited

**Officials in attendance:**

- David Bickerton, Director General, BEIS
- Tom Cooper, Director, UKGI

**Objective:** to meet with the Chair of Post Office Limited's (POL) Remuneration Committee (Remco); to discuss a recent breach of *Managing Public Money* in respect of a bonus paid to the CEO in 2021/22; to discuss POL's future pay proposals.

**Suggested agenda**

1. *Managing Public Money* breach
2. Retrospective approval of a change in the structure of the 2021/22 STIP
3. Approval of changes in metrics for the 2021-24 LTIP
4. Future pay proposals

**1. Managing Public Money Breach**

**Discussion points:**

- Thank Lisa for being proactive in her efforts to take control of the situation.
- Invite Lisa to talk through the steps that POL have taken/will take to ensure that there is no prospect of this situation arising again.

**Background:**

- On 4 October 2022, Lisa wrote to you recognising the seriousness of POL's *Managing Public Money* (MPM) responsibility and acknowledging that POL have breached this responsibility in making the CEO Short Term Incentive Plan payment without BEIS approval (further details of the breach are set out at **Annex A**).
- Lisa has noted that POL are taking steps to ensure that any ambiguity within POL about the approval processes are removed, so there is no prospect of this situation occurring again.

**2. Retrospective approval of a change in the structure of the 2021/22 STIP**

**Discussion points:**

- Thank Lisa for her letter and seeking your input on this critical matter.
- Note that Ministers will need to be strongly persuaded to approve any uplift to Nick's remuneration package outside of previously agreed parameters.
- Discuss the case for approval and whether this will be persuasive to Ministers.

OFFICIAL SENSITIVE  
COMMERCIAL

- Discuss the risks associated with not securing approval (e.g. asking the CEO to repay his bonus, and the likelihood of this precipitating his departure) and how these can be mitigated (e.g. CEO succession planning).

**Background:**

Lisa has sought Shareholder approval for a retrospective approval of a change in the structure of the 2021/22 STIP:

- agreement to make a payment to the CEO which – while within the maximum potential award agreed by ministers - is based on an alternative calculation to the one that was approved. POL argue that this change is important because it brings the structure of the CEO's STIP 2021-22 into line with the structure of the wider leadership's performance related pay.
- If this change request is not approved, the CEO will need to return around £30k. The CEO is considered a flight risk and we believe it is important to retain him to see through the public inquiry.
- We put a submission to you on this subject on 14 October 2022. You replied on 19 October 2022 noting that ministers are likely to reject the retrospective approval so it needs some further work.

**3. Approval of changes in metrics for the 2021-24 LTIP**

**Discussion points:**

- Discuss the proposed changes in metrics and whether these will be contentious to Ministers.

**Background:**

Lisa has also sought Shareholder approval for following changes in metrics for the 2021-24 LTIP:

- confirming the detail regarding the Customer Promise and Colleague Promise targets, which were yet to be determined when the outline framework and metric areas for LTIP 2021-24 were approved by Ministers in October 2021.
- Amending the financial gateway measure and cash flow metric in light of the outcome of the Spending Review settlement.
- We support the changes in these metrics on the basis that the original targets were unachievable given the funding constraints and economic conditions. These constraints have created challenges in addressing some of the key areas of Postmaster satisfaction – notably Postmaster remuneration

**4. Future pay proposals**

**Discussion points:**

- Ask Lisa to describe POL's future pay framework.
- Note that whilst POL raises strong arguments with respect to Nick's retention, Ministers will need to balance this against wider considerations.
- Note that whilst it remains POL's prerogative to put these schemes forward for Ministerial approval, POL should manage their expectations with respect to the likelihood of anything outside of previously established parameters being approved.

**Background:**

OFFICIAL SENSITIVE  
COMMERCIAL

- The next approvals which will be required for Executive Director pay will be STIP 22-23, LTIP 22-25. POL's future pay framework for CEO and CFO payments will require sign off from BEIS and HMT Ministers prior to taking effect. Further detail is in **Annex B** but at a high level the contentious issues to be put forward for Shareholder approval relate to the:
  - Cash Flow metric (schemes affected are **STIP 22/23, LTIP 22/25**).
  - Additional deferred STIP award (scheme affected is **STIP 22/23**).
  - Multiplier (scheme affected is **STIP 22/23**).
- The UKGI NED, Tom Cooper, has endeavoured through his role on Remco to align the shareholder interests to various remuneration schemes including CEO and CFO pay and their STIP and LTIP schemes. The UKGI NED's steers to Remco for each of issues listed above, prior to Remco taking the final decision on these, are illustrated in **Annex B**. However, we consider several of the metrics to be contentious, particularly around the multipliers and deferred element to the STIP 22/23 scheme.
- Ministers may take a risk averse approach to senior pay requests, especially in the context of the cost-of-living crisis, public spending cuts, the ongoing Statutory Inquiry, industrial action and widespread disquiet around postmaster remuneration.
- POL and UKGI believe there is some merit in putting forward the proposals for Ministerial consideration as POL has continued to flag that they believe the CEO is a flight risk and they have indicated that they will want to return to the broader question of his pay in due course. This is likely to be exacerbated by high inflation and increased wage demands; a benchmarking exercise undertaken by Willis Towers Watson shows that Nick could earn substantially more if he chose to move out of the public sector.
- Ultimately this is a judgement between the cost, and reputational damage, of paying more money to the CEO versus the risk of him leaving and the impact that will have on the company.
- We believe that Nick Read has played a positive role as CEO and that it is critical to have continuity in his role, particularly in the context of
  - a. the current change in Chair and three senior NEDs;
  - b. the policy review and review of POL financial sustainability; and in particular
  - c. the public inquiry into POL which means that the company is going to be under considerable stress for at least the next 18 months.

OFFICIAL SENSITIVE  
COMMERCIAL

## **Annex A: Managing Public Money breach**

### **BEIS/HMT approval requirements**

- POL, as a public corporation, is exempt from Cabinet Office spend controls. POL is also not subject to Civil Service Pay Remit Guidance and, other than as set out in the Articles, POL's Board retains operational freedom to make remuneration decisions in the best interests of the business.
- However, POL's Articles of Association requires Shareholder consent of "approval of or agreement to or any material variation or amendment to the remuneration paid or granted to any director of the company."
- The Post Office Shareholder is the Secretary of State for BEIS and their approval is required for Board remuneration. Moreover, the Chief Secretary to the Treasury (CST) must approve the remuneration arrangements for appointments to Public Corporations where performance related pay arrangements exceed the threshold of £17,500 and the appointment is a Ministerial appointment. The POL CEO and CFO are Ministerial Appointments.
- Remco Terms of Reference state that *"Executive Director STIP arrangements must be approved by the Shareholder."*
- The Framework Document states that *"The Remuneration Committee shall recommend to the POL Board the remuneration policy and any changes to individual elements of the remuneration packages for members of POL's Board. As per the Articles, the remuneration of all Board members will require approval by the Shareholder. Remuneration of Board members that exceeds the threshold set in HM Treasury's Guidance for Approval of Senior Pay requires additional approval by the Chief Secretary to the Treasury."*
- The need for approval applies to all material changes in pay arrangements including any changes which would increase pay above the agreed limits or even where pay stays within agreed limits but where the structure and metrics of the award differs materially from previously approved schemes.

### **MpM Breach**

- On 26 July 2022, RemCo agreed that POL should seek Ministerial approval for the revised CEO and CFO remuneration proposals on STIP21/22. This included a proposal to change the STIP 21/22 multiplier, effectively increasing the CEO's bonus calculation by £30k.
- The outturn for STIP 21/22 payment for the CEO/CFO was paid in late August 2022, despite necessary final Shareholder approvals on the revised structure of the scheme not having been sought as per RemCo's direction on 26 July 2022. The following table shows that Nick Read has received a £30k (or 23%) uplift on the amount payable as approved by Ministers. This may be considered a material change in the CEO's package in the context of the Shareholder rejecting the three previous requests to increase the CEO's salary. The change in STIP 21/22 rules made no difference to the CFO's bonus.

OFFICIAL SENSITIVE  
COMMERCIAL

STIP 21/22	Approved by Ministers		Paid (based on new multiplier approach)	Difference
	Maximum potential award	Award calculation based on actual performance		
CEO	£186,750	£132,894	£162,982	£30,088

- This is a failure in the required controls over public spending, known as a potential Managing Public Money (MPM) breach. This would become a public issue if POL accounts are qualified as a result and it can have serious consequences for those responsible.

OFFICIAL SENSITIVE  
COMMERCIAL

## Annex B: Future Pay Proposal issues

Cash Flow metric (schemes affected are **STIP 22/23, LTIP 22/25**)

- In the Chair's letter for the last two years, BEIS has asked POL to have a financial incentive based on cash flow (after deducting investment spend).
- Historically the financial metric has been EBITDAS (Operating Profit). UKGI proposed an 'EBITDAS – investment spend' (Operating Cash Flow) metric to take its place.
- Remco has since settled on a split metric of 75% EBITDAS and 25% Investment spend
- The Shareholder NED agreed with the split metrics proposed but disagreed with the 75/25 weighting. The 25% weighting places too little emphasis on investment spend control which is key to POL's financial sustainability. As only 30% of the STIP incentive and 20% of the LTIP incentive are weighted towards financial performance, a 75/25 split would translate to performance on investment spend only contributing to 7.5% of the overall STIP incentive and 5% of the overall LTIP incentive respectively.
- Therefore, the Shareholder NED is concerned that POL were not actioning Shareholder directives on pay incentives as outlined in the Annual Chair's letter in a satisfactory manner.

Additional deferred STIP award (scheme affected is **STIP 22/23**)

- POL's annual STIP and LTIP bonus schemes for the CEO and CFO are calculated through applying a fixed percentage of base salaries, with these percentages having been set and approved by the CST at the time of the appointments.
- POL's RemCo has approved the inclusion of an additional deferral element for the 2022/23 STIP as a one-off design feature to reflect market conditions and the intent to reward and retain talent.
- This means that the potential maximum pay-out under an individual's STIP for FY22/23 will be increased by 50%.
  - o The maximum pay-out of the CEO STIP, as approved at the time of appointment, is 45% of salary (£415k), so £187k. However, with the STIP22/23 Deferred Element, the maximum pay-out for CEO STIP 22/23 would increase to £280k.
  - o The maximum pay-out of the CFO STIP, as approved at the time of appointment, is 66% of base salary (£245k), or £162k. However, with the STIP22/23 Deferred Element, the maximum pay-out for CFO STIP 22/23 would increase to £242k.
- The total increase in CEO and CFO potential maximum aggregate remuneration for FY22/23 under the deferred STIP 22/23 scheme is illustrated below. The maximum award quantum for the Long Term (LTIP) bonus schemes will remain as previously agreed by BEIS and CST.
- The Shareholder NED disagreed with this proposal because while retention is important, this deferral would effectively substitute for the LTIP 20/23 which was cancelled as a result of COVID.
- Remco decided the deferral would not necessarily be included in future years.

Multiplier (schemes affected is **STIP 22/23**).

- In previous years a multiplier was applied to the personal performance element of the STIP. The STIP scheme was based on 80% financial performance (company EBITDAS) and 20% personal performance. A multiplier was then applied to the personal element reflecting the performance ranking of the individual.

OFFICIAL SENSITIVE  
COMMERCIAL

- For 22/23 STIP, Remco has agreed that a performance-based multiplier will be applied to the whole incentive earned (including the deferral element if awarded), thereby paying no account to the distinction between the individual and company specific performance components of the award. The rationale was to improve pay differentiation to reflect high performance.
- RemCo will also retain a discretion to adjust the level of the PDR multipliers as it sees fit. Currently, RemCo has determined that the multiplier should sit at 1.3x for exceptional performers (i.e. Performance Rating 5) and 1.1x for high performers (i.e. Performance Rating 4).
- This change will greatly enhance the potential OTE STIP payment for the CEO relative to previous schemes. The impact on CEO and CFO STIP awards are as follows based on RemCo's current set of approved performance multipliers:

Personal Ranking	Multiplier	CEO		CFO	
		OTE Earnings - New Approach	OTE Earnings - Old Approach	OTE Earnings - New Approach	OTE Earnings - Old Approach
3	1x	£124,500	£124,500	£97,920	£97,920
4	1.1x	£136,950	£126,990	£107,712	£99,878
5	1.3x	£161,850	£131,970	£127,296	£103,795

- The Shareholder NED disagreed with the proposal on the grounds that it would significantly increase pay to executives without improving performance. It would also potentially create a precedent to apply multipliers to LTIP awards, which have no individual performance-based components.
- As this is a material change to the structure of previous schemes, this will require BEIS and HMT ministerial approval to take effect.