

OFFICIAL SENSITIVE: COMMERCIALDepartment for
Business, Energy
& Industrial Strategy

Date: 11 June 2019

Director General: Gavin Lambert

Lead Official: Craig Watson

Lead Official Telephone: **GRO**

Recipient	To Note / Comment	To Approve / Decide
Greg Clark		X
Kelly Tolhurst		X
Permanent Secretary	X	
Special Advisers	X	

Post Office Limited litigation**Summary**

- At the industry meeting on 4 June, you (SoS) asked for advice on how the ongoing Post Office Limited (POL) litigation could be brought to a swift and satisfactory conclusion, ensuring postmasters who had been treated unfairly were appropriately compensated.

Timing

- Routine. Following the recent exchange of correspondence, Kelly Tolhurst is due to meet Tim Parker (POL Chair) and the board's new legal advisors to discuss POL's litigation strategy on 24 June.

Recommendations

- That you note the advice and our recommendation that you choose from the following options (which are not mutually exclusive):
 - Challenge the POL Chair and Board to review their litigation strategy, consider opportunities for early settlement and set out an action plan
 - Commission POL to carry out a project on how to structure and operate a settlement – including a fund which would subsequently assess claims, consider effect, and award compensation according to pre-agreed criteria
 - BEIS Ministers to state publicly that they want to see justice resulting from litigation for claimants with valid claims
 - Challenge Post Office to announce that it is taking on board some of the legitimate criticisms in the judgments to date and is taking action to address them
 - Put UKGI lead legal counsel (or another legal adviser) on the POL litigation sub committee as director or observer
 - Invite Nigel Boardman, chair of the BEIS Audit and Risk Committee, to carry out some independent due diligence on POL's litigation strategy
 - Put in place clear information-sharing arrangements via the proposed Framework Agreement for POL.
- More radical steps are presented in options 8 -10; we recommend these are not pursued at this stage.

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5. We have talked through these issues with Kelly Tolhurst, who is keen that POL management takes active steps to address Ministers' concerns. Kelly will attend the POL Board meeting at the end of July and this will be an opportunity to raise these issues directly with the Board.

Advice

Latest position of the current litigation and current POL strategy

6. The litigation has been broken down into four trials scheduled between November 2018 and March 2020. The current status of the litigation is that at a hearing on 23 May the Judge denied POL permission to appeal his judgment in the first "Common Issues" Trial and awarded the Claimants their costs of the Common Issues Trial rather than reserving this judgment until later in the litigation. Setting out his reasons in a written judgment of 4 June, the Judge criticised POL's conduct again, namely POL's "veiled or implied threat that mirrors the approach adopted by Post Office on the recusal application, namely that in adopting a course of action in the face of opposition by the Post Office ... runs the risk that the Post Office will say that the overall outcome of the litigation ... has already been decided". The Judge also expressed concern about the escalating costs of the litigation overall – he puts the figure at over £13m for POL, including £500k for the failed attempt to get the judge recused.
7. POL will now apply directly to the Court of Appeal by its 13 June deadline and, after reviewing its approach under the new legal team, will narrow its focus onto the most material legal issues affecting its contract with Postmasters. If the Court grants permission, the appeal will likely be heard within the next 12 months while a refusal will mean that the original judgment stands. The part-heard second "Horizon Issues" Trial concerning the function and reliability of the electronic accounting system (Horizon) used by Postmasters resumed on 4 June with expert evidence and is expected to conclude on 2 July, with the judgment expected several months later.
8. The Board has a litigation sub-committee to oversee its litigation strategy, which is chaired by Tim Parker and attended by Shareholder NED Tom Cooper. Following the adverse and unexpected judgment in the first trial on the "Common Issues" POL took additional external legal advice prior to pursuing the recusal, which subsequently failed. POL's Board decided that new legal leadership and a wider review of its strategy was required; they replaced the company's General Counsel and appointed new legal advisors (Herbert Smith Freehills) to advise them directly on their litigation strategy. A new QC has also been appointed.
9. The Claimant group involved in the litigation is large, with 561 Claimants involved. While POL has information on some of the cases from a previous mediation process, the Claimants have never properly quantified their claim making it difficult to estimate potential liabilities accurately but POL's new legal team are reviewing settlement and likely outcomes from the litigation, including potential costs, and will discuss these with the Minister when they meet. We will ensure POL provide clear written briefing, including on settlement strategy, in advance of that meeting.

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10. To note, POL's auditors have raised a concern previously that no figures are included in the accounts on the potential liability. Providing these figures to BEIS could result in two consequences:
- any figure provided to BEIS having to be disclosed to the auditors and in POL's accounts. If that happens, this could potentially set a floor for any settlement negotiations;
 - it could raise a going concern issue due to POL's inability to fund any large settlement, which could lead to the auditors looking to BEIS to provide a letter of comfort that it will fund any settlement.
11. Should POL settle the existing case, there is a chance that additional Claimants may come forward so there may be a further and ongoing liability. We will ask POL to provide an assessment of this risk in their briefing.
12. In addition, some of the Claimants may not have valid claims; for example, some have pleaded guilty to criminal charges in the past. Therefore, in considering options, including settlement, to resolve the litigation POL will need to consider a process to determine which cases are genuine. With so many claimants, and the strong personal feelings aroused by the cases, it may prove difficult in practice to settle all aspects at acceptable cost without wasting public money on rewarding bad behaviour. Financial payments would have to satisfy Managing Public Money criteria and would require Ministerial and HMT consent.
- Powers available to the SoS as sole shareholder***
13. The Postal Services Act 2011 provided for a "Post Office company" to continue to be owned by the Crown after the privatisation of Royal Mail. On separation, the Secretary of State was granted a Special Share in the Post Office and the rights and privileges this conveyed are set out in the "Articles of Association". The Shareholder is entitled to attend and speak at any general meeting or any meeting of any other class of shareholders of POL, but the Special Share does not carry voting rights or any other rights at any such meeting. The prior written consent of the Shareholder is required for certain decisions, which generally relate to appointments and remuneration, strategic planning, asset sales and commercial decisions, large payments and borrowing. These arrangements ensure that the Shareholder can influence key strategic decisions, without the need for day-to-day involvement in the operations of the Post Office or the management of its branch network and staff.
14. As sole shareholder, Government sets the strategic framework for the Post Office, in particular providing a minimum, accessible, branch network in a way that is sustainable for the taxpayer. POL is a large and complex business – the largest retail network in Europe, and as such it is given the operational freedom to deliver on its HMG-set objectives as a commercial business. Under the Articles of Association, SoS approval is required for a number of reserved matters including board appointments and remuneration and expenditure over £50m. This does not include explicit powers to direct the board to take a specific course of action,

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though ultimately Ministers have the right to appoint or remove any member of the board, including the two executive members of the Board (CEO and CFO), which could effectively be used as a lever to steer the board in a particular direction.

15. As you are aware, a competition is currently underway to recruit a permanent CEO and panel interviews are due to take place early this week.
16. While it is perfectly proper for the shareholder to express views and ensure the Board understand their position, care needs to be taken that Ministers do not risk being regarded as shadow directors. A shadow director is someone in accordance with whose directions or instructions the board are accustomed to act. A shadow director effectively has the same legal duties as a normal director and can potentially incur personal liability for their actions.

Potential options available

17. The table at Annex A sets out the advantages and risks of a range of options Ministers could take to address concerns over the management of the ongoing litigation. These range from challenging the existing POL Board to change their litigation strategy to more fundamental changes such as replacing the POL Board or BEIS assuming control of the litigation strategy.
18. More vigorous action carries greater risks, as flagged in Annex A. Forcing further changes to the leadership team will risk disrupting the progress POL have been making in other areas of the operation of the business, including transforming the business from loss making to returning a profit for the first time in 16 years. Making public statements or directing POL to take certain action could weaken their negotiating position in relation to settlement and make it harder to stick to the existing BEIS line that this is an operational matter for POL.
19. **We recommend that you choose from options 1 – 7 (either individually or collectively) as the most appropriate actions to take at this stage.** Taking these actions would send a clear signal to POL on the direction Government would like the litigation to take, without exposing Ministers to the legal risk of acting in a manner that may be characterised as a shadow Director and without opening the department up to additional financial exposure. Should Ministers wish to pursue some of these options, we recommend they are raised by Kelly Tolhurst in her meeting with POL on 24 June. We recommend a final decision on the more fundamental options (options 8 – 11) should await the outcome of this meeting.

Timing and potential settlement windows

20. Should you decide you wish to encourage POL to settle the case at the earliest opportunity, they will need to identify the most appropriate time to begin settlement discussions with the Claimants. Again, we will ask POL to cover this in the briefing they provide for the forthcoming meeting.

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21. The Daily Mail has recently taken on a campaign to 'Save our local Post Offices', which has included one story on the impact of the trial. However, the litigation does not feature as one of the paper's five demands. There has also been low level reporting mainly in the trade media, specifically Computer Weekly, of the Post Office litigation.
22. There is pressure from the Daily Mail campaign for the government to be seen to be sympathetic to the plight of postmasters generally. and a carefully worded statement would be a good opportunity to convey Ministerial support for them, without showing public conflict with the Post Office.
23. If considered appropriate, we could inform the Daily Mail if options 1, 2, 4, 5 or 6 were taken as this would demonstrate that BEIS was taking an active role in the matter and is sympathetic to the claimants. However, any failure to then significantly alter the Post Office's approach to this litigation risks BEIS being seen as complicit or powerless.
24. Option 3 would require careful wording, which we can advise on. Again, should the litigation fail to change course significantly, the SoS could be left open to further questions and criticism.
25. We agree with policy colleagues in advising against options 8 - 11. SoS going public with a view against the Post Office could lead to coverage of an outright conflict between the two organisations. This could also add fuel to the Daily Mail's campaign, which we are working hard with Special Advisors and the Post Office communications team to bring to address, working with their key correspondent.
26. Once a decision is reached, we will work on the necessary communications with policy colleagues and Special Advisors.

Accounting Officer considerations

27. POL have previously advised both Ministers and the Permanent Secretary that they could fund any settlement or compensation awarded of between £30m-£50m from their own resources and possibly more. Anything above this they are likely to need support from BEIS with (on the assumption that their social purpose targets remain the same). The department does not currently have any spare budget available to support such a funding requirement. However, there are other options; for instance, raising funds from sale of non-strategic ancillary businesses such as POL's telecommunications business.
28. There are a number of Accounting Officer considerations across the range of options that we have presented. These are included in the attached annex and include risks around the legal, affordability and value for money of any option. We will develop full Accounting Officer advice once you have indicated your preferred option going forward.

Contributors

29. This advice contains financial considerations, as agreed with Richard Beckett.

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30. Legal Richard Watson (UKGI) and Jane Corera (BEIS) have been consulted and agreed the content of this advice.
31. Communications considerations have been taken into account and agreed with Annabelle Miles.
32. This advice does not have parliamentary handling implications at this time, as agreed with Craig Watson.

Annexes

- A. Options for Ministers to consider
- B. Summary of changes in personnel in POL over last three years