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UK Government Investments

OFFICIAL - SENSITIVE

Department for Business, Energy & Industrial Strategy

To: Sarah Munby
From: Siv Rajeswaran (UKGI)
SCS clearing: Tom Cooper (UKGI); Rob Brightwell (BEIS)

Meeting Brief: Introductory Meeting, Henry Staunton (Chair, Post Office Ltd)

Date, time & location of meeting: January 3, 2023

Meeting attendees:
- Sarah Munby
- Henry Staunton

Official(s) attendee(s):
- BEIS/Private Office to confirm

Agenda:

Item 1: CEO Pay

Item 2: NED Appointments

Item 3: POL Finances and Three-Year Plan

Item 4: Recent Correspondence

Item 5: NI Energy Bill Support Scheme

Item 6: AOB / other live issues

Overall objective / why is this meeting happening?
- An introductory meeting with the incoming Chair of Post Office Limited (POL), Henry Staunton. An opportunity to discuss the priorities set out in the Chair's letter, as well as other live issues.
- Although he has been in post for less than a month, it would be useful to get his first impressions

1. **CEO Pay**

Objective: SoS will meet with Henry Staunton on 9 January 2023 where it is expected Henry will raise the implications of any adverse decision on the 2021-22 bonus request. It is also expected that SoS's considerations around CEO pay will be raised directly with the Chair in their meeting scheduled for 9 January. Perm Sec may wish to prep Henry for his upcoming meeting with SoS.

<u>Retrospective approval for STIP 21/22 payment to Nick Read</u>

- SoS has rejected POL's request to bring the structure of CEO's 2021-22 performance pay into line with other members of POL senior management. <u>This has not been communicated to POL</u>.
- The increase requested by POL was worth £30,088. POL should have sought BEIS Ministerial approval for this change before making the payment.
- Net of tax, the CEO would have to repay £16,548 if the decision not to approve cannot be reversed.

- The outstanding repayment issue has also meant that POL will fail to meet its calendar year deadline to file accounts with Companies House. This is because the CEO's pay for 2021-22 is set out in the remuneration report of the POL Annual Report and Accounts 2021-22.

CEO Remuneration Package

- On 14 November, the Chair wrote to SoS requesting approval to increase the CEO's remuneration in line with the benchmark lower quartile. This has three components: (i) increase base salary by 29% to £535,800; (ii) increase LTIP to 60% at target or 100% at stretch; and (iii) increase STIP to 50% or 90%. Total remuneration would be £1,125,180 at target and £1,553,820 at stretch.
- On 5 December, SoS and Minister Hollinrake advised that they did not support the Chair's proposal. This has not been communicated to POL.

2. NED appointments

Objective: An exercise to recruit three new NEDs to replace board members whose terms end in 2023 is underway. Perm Sec may wish to seek out Henry's views and assurances on the prospective candidates and their cultural fit for the Board and POL's future commercial strategy. The preferred candidate for the ARC Chair role will not improve the diversity of POL's board. The shortlist for the Remco Chair role is all female.

- The advertised positions pertain to the Remunerations Committee Chair; Audit, Risk and Compliance Committee Chair; and Generalist NED positions on the Board respectively. All three departing NEDs are female.
- POL has completed the first round of interviews and has identified strong candidates for the positions of Audit, Risk and Compliance Committee Chair and the Generalist NED. It is expected they will complete due diligence and put forward a formal appointment recommendation for approval by Ministers in the first Ministerial Box of 2023.
- A shortlist has been agreed for the Remco Chair.

3. POL Finances and Three-Year Plan

Objective: The risks around the 3-year plan have already been surfaced, as has the more positive intra-year position. Perm Sec may wish to probe on: what magnitude of further downside might crystallise around mails – particularly driven by Royal Mail strikes; what upside may exist in the Bank of Ireland business given higher interest rates and; what assurance POL can offer than further cost escalation won't impact key projects (NBIT, legal spend) given the very large movements in less than c.9 months following the post-SR settlement position.

POL Short term finances

- Current year performance for POL has been positive compared to their 22/23 budget, with a year-to-date position of £21.5m trading profit against a budget of £1.6m (at period 7; end-September). However, this large outperformance should be viewed with significant caution.

- Much of the upside so far is due to the post-pandemic travel recovery (driving travel insurance and foreign exchange upsides). These factors are all forecast to, or already are, declining with pressures to consumer spending, inflationary and recessionary headwinds, and a lack of certainty over comparable energy bill schemes going forward.
- Underlying weakness in the core Mails business is substantial and increasing. Year to date performance is £11m below budget (c.£181m revenue vs c.£192m budget). The Royal Mail strikes will harm peak trading periods around Black Friday and up to Christmas and have longer term effects if customers do not return to Royal Mail.
- As a result of poor Mails performance, early suggestions are that further actions on Postmaster remuneration may be needed to support network stability. POL acknowledges that this would sit uncomfortably alongside the current discussions on funding for POL itself

Three-Year Plan

- POL continues to work on an updated 3-year plan to be delivered in February and the funding ask of Government, Nick Read has recently written to you to indicate the required funding is likely to be at least £160m and could be substantially higher
- POL has signalled that the position has deteriorated materially in the last 2 months. Substantial cost increases to NBIT (lifetime cost at least £240m compared to £140m at SR) and legal spend (c.£90m increase vs SR position) alongside projected deterioration in profitability (c.£160m driven mainly by mails, potential for further deterioration) are the most significant factors.
- NBIT costs are being reviewed because POL believes the rollout of the new system will be significantly more expensive than originally planned. This is partly a result of the Inquiry's examination of Horizon's rollout in the late 1990s.
- Legal costs remain a significant concern, particularly in relation to the Inquiry which the business has signalled could be £90m. IRRELEVANT IRRELEVANT POL has not been able so far to explain in any detail the reasons behind the dramatic increase in the cost estimates that have taken place this year. POL does not appear to be using the financial model that was built last year with support from KPMG at significant cost.
- Key next steps will involve crystallising a more certain number alongside a full plan and engaging with BEIS Finance and HMT colleagues to explore remedial options

4. Recent Correspondence – CEO Letter, Chair's Letter, Historical Matters, ARAC Chair's Letter

Objective: Perm Sec to note the current status of the recent exchange in correspondence between senior officials of POL and BEIS

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Nick Read Letter – Three Year Plan (December)

- Nick Read has written outlining the likely financial shortfall over the 3-year plan. POL now expects a shortfall of at least £160m over the 3-year period.
- The letter also flags non-financial risks around delivery, given the fatigued workforce, heightened risk profile and need for some level of network transformation.
- POL notes that areas of higher spend either directly or indirectly link to the Inquiry and therefore 'cannot be delivered badly'
- POL also flags a desire to borrow £50m in order to complete the DMB refranchising program.

Chair Letter and Response (December)

The Chair has written providing an update on progress against shareholder priorities of financial performance, Cultural Change and Historical Matters. Key points to note with respect to POL's stated performance are as follows:

- Financial Performance: While the letter cites an aim to protect medium term viability of POL through cost / revenue focus, we already know from the wider 3-year plan discussions that POL will require substantial additional HMG funding to remain viable within the next 2.5 years.
- Cultural Change: the letter asserts that POL *continues to make good progress with organisational and cultural reform to ensure that there is sufficient capacity, capability and resilience at all levels of the business including the top team.* Certainly, some improvements have been made, including the appointment of a new Group Chief People Officer (Jane Davies) in December. However, the NFSP continue to complain that POL are not doing enough to repair the relationship, and work collaboratively, with postmasters. The ongoing Horizon IT Inquiry is also cited as a barrier to attracting talent, particularly in the already competitive field of IT (although the Group Chief Digital and Information Officer, appointed in May of this year, performs highly).
- Overturned Historical Convictions: Steady progress continues to be made on compensation payments. Non-pecuniary claims are being progressed and settled at pace following Lord Dyson's Evaluation (29 to date). Pecuniary claims have been trickier (two settled to date) due in part to unexpected delays in claimants bringing forward their claims however POL is progressing test cases to put in place a framework from early-2023. In total, c. £13m has been paid so far.
- Historical Shortfall Scheme: POL hit its end of year target of 95% of offers issued from the original HSS cohort (2,244; £74m offered; £46m paid). Focus is now on the making offers for the last remaining complex cases (e.g. insolvency / bankruptcy-related) by March '23, resolving disputes and delivering late application claims.

POL ARAC Chair to BEIS ARAC Chair (December)

- The POL ARAC chair, Carla Stent, wrote to Vikas Shah to flag that a number of Post Office risks are beyond tolerance. These include:
    - Cyber-attack risks resulting in the loss of availability of critical systems.
    - An inability to extend the Fujitsu contract, a risk if NBIT does not deliver on time
    - Poor management of unstructured information meaning not DPA compliant.
- Post Office asserts that these risks will remain out of tolerance until its funding position improves. They have invited Vikas to attend a POL ARAC meeting. Clive Maxwell has been alerted to this letter

<u>Historical Matters Letter (September)</u>

- Before stepping down as Chair in September, Tim Parker wrote to you regarding the Common Issues (CIJ) and Historic Issues (HIJ) Judgements. It was agreed that we would pick up the substance of the letter when the new Chair was in post.
- This action was required by the 2022/23 Chair's Letter which stated that a key objective for POL's current Board and management team is to demonstrate to the Inquiry's satisfaction that changes have been, or are in the process of being, made to POL's systems and processes so that they are fit for purpose, and that the Chair should write, by the end of the parliamentary summer recess, to let you know what assurance, both internal and external, the Board is putting in place to demonstrate this.
- Tim Parker's letter demonstrates there has been progress in delivering actions in response to the CIJ and HIJ. But, overall progress has been significantly slower than planned. POL's management is preparing a paper for the January Board meeting. We have proposed that POL provide an update following that meeting and will delay a substantive response until then. External assurance has yet to be scheduled and this remains a concern.

5. NI EBSS

Objective – Perm Sec to thank POL for working to deliver the Energy Bill Support Scheme (EBSS) energy bill support to consumers in Northern Ireland (NI). It might be helpful to share your reflections on the process and listen to any concerns Henry may have. [If needed] to discuss the tensions that emerged during the process.

- Post Office will help deliver the EBSS in NI by enabling customers who do not pay their energy bills by direct debit to exchange vouchers for cash at a post office – mirroring their role in delivering the scheme in GB to date.
- There have been occasional tensions between the policy ambition and POL's capacity to deliver; notably they were asked to collaborate with PayPoint on a digital redemption option. POL's view was that this would introduce delay and increase risk for minimal benefit; they also cited the

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strategic impact of supporting a direct competitor in challenging their market share without having to bear the delivery risk.

- SoS accepted that he should not force POL into a partnership but expressed his disappointment at the outcome; he has asked to visit PayPoint, which is based in his constituency, in the new year.
- We understand that POL's stance may have left Ministers and Senior officials with the impression that the company has been uncooperative and has acted as a barrier to innovation. At the same time, working level contacts have expressed disappointment that BEIS did not appear to be on their side in this matter given the lengths the Company has gone to in support of a key policy.
- The Policy Team is keen to explore ways in which POL could proactively present a more positive side of their operations to Ministers, and we are working with our contacts on some potential visit options for the new year.