

PS Oliver Page

Date

**Meeting with Tim Parker** IRRELEVANT **1 Victoria Street,  
3pm to 3.45pm, Thursday 31<sup>st</sup> October**

**Purpose**

- Following September's UKGI Board, you agreed to meet Tim Parker to reinforce the Department's priorities for POL, including a commitment to cultural change.

**Attendees**

- Tim Parker, Chair, Post Office Limited
- Tom Cooper, UKGI NED Director for POL
- Carl Creswell, Director BEIS Post Office Policy Team

**Our objective**

- To ensure Tim understands our desire to see cultural change at POL, and a robust 5 Year Plan based on financial self-sustainability and effective control of investment spending.

**Their objective**

- Tim is expecting to be in listening mode, to understand your concerns. He will want to reassure you that he is fully supportive of Nick Read and his review, and is focused on the litigation case.
- Tim should confirm that the company will introduce a significantly greater degree of flexibility into the pay arrangements for periods starting on 1 April 2020. These changes will allow reductions to LTIP payments (in addition to grants) as well as clarifying the degree of discretion relating to STIP.

**Issues**

- Litigation: Judgment in the Horizon trial is expected in early November, following the discovery that POL had failed to disclose information ("Known Error Logs" or KELs) that may provide a fuller account of bugs in the Horizon system. While this appears to be Fujitsu's responsibility, Justice Fraser is likely to be highly critical of POL. A decision on POL's application to appeal the Common Issue trial is expected 12 November.
- Mediation is currently scheduled for 27-28 November and POL is working on the amount to offer claimants that haven't been convicted. There is also a debate about how to approach convicted claimants.
- In relation to culture, Nick Read is launching a McKinsey Organisational Health Index survey aimed at employees. Similar research is being undertaken with customers and Postmasters. The purpose is to obtain much better information to inform specific actions and measure progress. This forms part of Nick Read's 'Purpose, Strategy and Growth' review that he described to you when you met, and which is due to complete in January. It will take account of the Department's work on the long-term policy vision.
- The BEIS Select Committee's report "recommend[s] that the Government undertake an urgent review of its mechanisms for holding Post Office Ltd to account".
- POL is considering announcing an increase in Postmaster pay of approximately £30m per annum.
- There is likely to be a Royal Mail strike in the run-up to Christmas. POL is working with RMG to prepare.
- POL is planning to market the Telecoms business with a view to a sale, to complete in the first half of 2020.
- POL is minded not to bid for DWP's replacement product for POCa, which is a voucher-based system.

**Background**

- The discussion at UKGI's September Board focused on weaknesses in the company's culture, in particular its handling of the litigation and relationship with postmasters.

**Briefing**

- See overleaf.

## AGENDA FOR MEETING – ISSUES TO RAISE AND POINTS TO MAKE

Agenda Item:	Issue to raise and points to make:
<b>Culture</b>	<ul style="list-style-type: none"> <li>• POL's culture needs to change and, as the shareholder, we expect the Chair and Board to be leading this.</li> <li>• The leadership's decisions on the litigation (such as the failed, expensive recusal attempt) and the proposal to pay bonuses in full appeared tone-deaf and complacent.</li> <li>• When you met Nick Read, you underlined the need to think hard about what the leadership decisions said about POL's culture. You encouraged Nick to use that as an opportunity to accelerate change, perhaps measuring staff reactions.</li> <li>• Welcome Nick's positive start, his focus on obtaining real data to inform decisions, including from postmasters and customers, and his engagement with BEIS/UKGI.</li> <li>• Tim often gives the impression that he thinks Government is too interventionist. The BEIS Select Committee's calls for stronger Government 'mechanisms for holding the Post Office to account' challenges this and shows why it matters.</li> <li>• We hope to see culture change embedded within Nick's vision for Post Office and the 5 Year Plan. You could commission a report to you on this (perhaps in January, after Nick's work).</li> </ul>
<b>Litigation</b>	<ul style="list-style-type: none"> <li>• Resolving the litigation is going to be very high risk, not least for POL's reputation.</li> <li>• You might want to underline the point that you made to Nick that there is likely to be anger and indignation in the event of a negative judgment so POL should try to get ahead of this.</li> <li>• POL has been clear that it is taking the settlement discussions seriously. You could ask Tim to update on the likely cost and the approach to both convicted and non-convicted claimants</li> </ul>
<b>5 Year Plan</b>	<ul style="list-style-type: none"> <li>• POL's 5 Year Plan should challenge the business to drive revenue and efficiencies. Needs a clear aspirational target.</li> <li>• We may need external assurance of the underpinning numbers.</li> <li>• A strong case will need to be made for the continuation of subsidy, as our (and HMT's) starting point is zero. POL also needs to deliver a mechanism to return value to the taxpayer.</li> <li>• Needs to link to BEIS long-term vision work, also looking at the network requirements and POL's social purpose.</li> <li>• The projections in POL's 5 Year Plan to reduce costs are insufficient to fund the investment required to ensure sustainability. Digital Identity, Insurance and other financial services need investment, as do the company's IT and systems.</li> </ul>
<b>Change spend</b>	<ul style="list-style-type: none"> <li>• In our view, the company and Board has been too focused on achieving EBITDAS targets and not sufficiently attentive to change spend and execution.</li> <li>• STIP and LTIP should be redesigned to reward cash flow (after change spend) as well as profits.</li> </ul>
<b>Board and management</b>	<ul style="list-style-type: none"> <li>• What are Tim's views on the management changes that Nick is likely to make in future?</li> <li>• It would be helpful to check with Tim that he has sufficient</li> </ul>

- |  |  |
|--|--|
|  | <ul style="list-style-type: none"><li>• time for POL given his other commitments</li></ul> |
|--|--|

### **Organisation and biographies**

Tim Parker was appointed as Chair of POL in October 2015 and re-appointed for a four-year term in October 2018. He also Chair's POL's Nominations Committee and is a member of its Remuneration Committee. Tim has been CEO of several well-known companies: Kenwood, Clarks, Kwik-Fit, the AA and Samsonite. He has served as a Non-Executive Director on several FTSE 100 companies: Legal and General, Alliance Boots and Compass Group, and has been a Board member of the Audit Commission and the South West Regional Development Agency. He has been an Industrial Partner at CVC Capital Partners. Tim is the Executive Chairman of Samsonite Corporation and Non-Executive Chairman of the National Trust.

Alex previously met Tim on 5 March 2019 to discuss a variety of operational and strategic issues faced by POL, including the ongoing litigation.



**ANNEX: More detailed points that you could make****Corporate Culture****Lines to Take**

- POL's culture needs to change, especially among the leadership group but also in its relationship with postmasters.
- Welcome Nick Read's intention to refocus the business on postmasters and customers and to obtain real data on their views to inform decisions. Important for UKGI/BEIS to be involved.
- Culture change should be embedded within Nick's new vision for Post Office and the 5 Year plan

**Key messages**

- Several issues have come together to cause us concern: the approach to the litigation; the generally poor relationship with postmasters; and the insensitivity to political concerns demonstrated by the Bonus issue.
- This causes political concerns for Ministers, but also it is a business problem if it weakens the brand and the sustainability of the network.
- Recognise and welcome the steps already taken, e.g. changing the legal team, reviewing agent pay, the CEO engaging staff across POL to seek their ideas.
- We want POL to be commercially sustainable, but with a social purpose. The environment it operates in means it will be held to higher standards than other commercial entities.
- POL needs to demonstrate that it recognises the culture problem, are taking steps to investigate it and are committed to change. What we want to see is:
  - A leadership team that combines strong commercial skills with a more demonstrable sense of its civic duty as custodians of a much-loved and crucial institution.
  - Better relationships with postmasters and a focus on ensuring that running a post office is an attractive proposition.
  - More savviness when it comes to consulting on changes (e.g. franchising).
  - A stronger strategic approach so that problems are identified and avoided rather than dealing with them after they have happened.
  - Openness, rather than defensiveness, about misjudgements and mistakes, so that lessons can be learned for the future.
  - Welcoming of the shareholder's involvement and transparent (both about data but also in giving us key information in advance of events).
- There's a lot to learn from other organisations that have gone through change programmes.
  - Engaging with stakeholders and getting real data– welcome Nick's initiatives here
  - KPIs around culture change, for example: workforce engagement, postmaster turnover rates, customer satisfaction, trust in the brand
  - These could be linked to remuneration too (as they are in RBS)
  - Stronger engagement from the Board with its stakeholders, especially postmasters
- Nick Read has launched a "Purpose, Strategy and Growth" review, working with McKinsey, which will clarify POL's purpose, vision and values. As part of this, POL has launched an Organisational Health questionnaire to all staff, so that decisions can be based on real data. Similar processes are being planned to engage with postmasters.
- We know that POL has to own this for it to be effective, and it should be embedded within Nick's new vision for Post Office, and the 5 Year Plan. POL (Nick Read and Al Cameron) are due to present emerging findings from his review to BEIS/UKGI at a Shareholder Meeting on 13 November. You could ask to discuss the final plan with Tim and Nick in the New Year.
- Importance of aligning POL and BEIS's vision for the future. If we are aligned about what is important then we'll back you in future.

### **Additional background**

- The reduction of executive bonuses was reported in the [blog](#) of Nick Wallis, an independent reporter who is providing extensive coverage of the litigation trials (attached Annex A).
- Remco has discussed and in principle agreed measures to provide significantly greater discretion on bonuses in future. The company's ability to exercise discretion in a very wide range of circumstances has been clarified. Importantly, in relation to LTIP, discretion would apply to payouts as well as grants. Based on legal advice received, these changes would come into effect for 20/21 STIP and 2020/23 LTIP performance periods. In relation to the 2019/20 STIP, the company already has a significant degree of discretion as demonstrated over the summer. Remco was advised that to amend the 2019/22 LTIP would breach contractual entitlement.



## Litigation

### Lines to Take

- Resolving the litigation is going to be very high risk, not least for POL's reputation
- There may be anger in the event of a negative judgment and POL should try to get ahead of this
- POL has made it clear in Court that it is taking the settlement discussions seriously. You could ask Tim for an update on where things stand, the likely cost and the approach being taken

### Background

- POL is still waiting for judgment in the second trial ('Horizon') and Mr Justice Fraser has indicated he hopes to hand down in early November. As with the first trial (Common Issues) the POL Board, including Tom Cooper as UKGI NED, will have advance notice of the judgment although they will not be able to share its contents until it is made public. POL and BEIS comms will work closely together when the judgment is handed down.
- On 12 November, the Court of Appeal will hold an oral hearing on POL's application for permission to appeal elements of the judgment in the Common Issue trial. A decision on whether POL will be granted permission to appeal is expected soon afterwards.
- The date for the third trial has been set for March 2020. It will consider "measure of loss" questions only, based on assumed facts. In brief terms, this means the Court will be asked to consider whether certain heads of loss are recoverable in principle, subject to proof of breach and causation in due course. The court has set a timetable for the steps the parties must complete to be ready for this trial. Any agreed mediation can take place in parallel with this timetable.
- Whilst awaiting the judgement of the Horizon trial, POL informed us that a disclosure incident arose in relation to "Known Error Logs" (KELs) supplied by Fujitsu that were key documents specifically in relation to the Horizon trial. POL have made the Court and Claimants solicitors aware and are working with Fujitsu to understand the extent to which the information they discussed during the trial was accurate. POL have advised us that their analysis of the previous versions of the KELs disclosed at trial has been completed with 25 containing new information though in their view they do not present any material concern or change to their submissions made at the Horizon Issues Trial. Disclosure has been made to the Claimants and POL await their substantive response.
- The discovery of these KELs will provide a fuller account of any 'bugs' in Horizon that occurred in the past and were fixed. To the extent that they are materially different from those disclosed in the trial, they may bear on the subject of that trial, namely the integrity of the Horizon system. The Judge is likely to be highly critical of Post Office and it possible that he may order a partial or full retrial, at POL's expense.
- Mediation - POL's legal advisors have been making preparations for a mediation scheduled for 27-28 November 2019, including work to understand and verify the magnitude of potential claims and the range of possible settlement figures. We remain concerned about how POL should deal with the convicted claimants (61 of the claimant group of 551), particularly as for many they will likely be in the same factual position as non-convicted claimants i.e. they got into a muddle because of Horizon issues and lack of training and support, tried to cover this up and then pleaded guilty to false accounting to avoid more serious charges. POL's current advice is not to mediate with convicted claimants until the outcome of the Criminal Cases Review Commission process is known. Only the Court of Appeal can overturn a conviction once a case is referred to them by the Criminal Cases Review Commission.
- UKGI and BEIS have established an internal Working Group with HMT to discuss preparations and clearance processes for a possible settlement. Nigel Boardman (BEIS Board member and ARC Chair) is on that group, which met on 15 October. Nigel was also tasked by Ministers to provide some due diligence around POL's litigation strategy and met with POL and their legal team in September. He is meeting Kelly Tolhurst on 30<sup>th</sup> October to provide an update.

- For any spend over £50m POL are required to seek Shareholder approval. Given any potential settlement would be considered novel and contentious, even if below the £50m threshold, UKGI will provide specific written advice for Ministerial approval on any proposed settlement by POL.

## 5 Year Plan

### Lines to Take

- The POL 5 Year Plan should challenge the business to drive revenue and efficiencies. We would like to see a clear aspirational target, akin to the £100m EBITDAS target of the current 3-year plan
- We may need external assurance of the numbers underpinning the plan.
- A strong case will need to be made for the continuation of subsidy. POL also needs to deliver a mechanism to return value to the taxpayer.
- The company's current plans to reduce costs are insufficient to fund the investment it needs.

### Key messages

- In the first iteration of the 5YP, POL does not generate net cash to pay off debt over the period. It's cash negative for the first 2 years or so and then turns cash positive for the rest of the period but overall it is more or less neutral.
- Non-staff expenses aren't falling over the period by as much as we might expect.
- Although EBITDAS is increasing, it all gets absorbed by change spend and that's what seems to lead to no net cash flow.
- Overall, EBITDAS margins look reasonably healthy and if the company were a retailer for example, you'd expect the business to be able to generate healthy cash flow even after reinvesting in the business. POL still has a lot of catching up to do to bring the technology up to date and some allowances need to be made for that.
- It might be helpful to perform some benchmarking to see if we can set a top-down aspiration for the business and then see if the bottom-up work can get somewhere close. POL's current 3-year plan has an aspirational target for £100m EBITDAS, which has been effective in focusing management on the turnaround and restructuring. We propose moving away from EBITDAS in future because it doesn't capture change spend very well or balance sheet efficiency.
- Keen for Nick's review to link with BEIS's Long Term Vision work and particularly on understanding the case for a post 2021 subsidy. The starting point is for zero subsidy.

### Additional background

- POL has started work on a 5YP which was discussed at the Board's July away day and with UKGI. Work has paused pending the outcome of Nick Read's "Purpose, Strategy and Growth" (PSG) review. The first draft was viewed as overly optimistic and is likely to be made more realistic in future iterations.
- It is important that this review dovetails with BEIS' long term vision work which covers:
  - Approach to funding and commercial sustainability: whilst the starting point for a post 2021 subsidy is zero, in line with HMT expectations, BEIS are exploring the case for a post 2021 'subsidy with conditions'. The purpose of this is to build a stronger evidence base particularly on the costs and 'social value' benefits associated with loss making branches and to develop a stronger VfM rationale for any future HMG funding.
  - Ensuring the sustainability of the network and positive workforce relations: BEIS will work closely with POL to consider the outcomes of the PSG review and how it addresses the issues raised in the Select Committee report (Annex C) and by stakeholders such as NFSP and Citizens Advice. It will also include reviewing the size of the network, and the definition of a branch, in light of the significant increase in outreaches.
  - Redefining the role and value of the social purpose: BEIS will work with POL to collect data on the uncommercial branches (including community branches) ahead of the SR alongside consolidating a wider evidence base that draws on innovative local best practice. This will help inform the definition and measurement approach of the social



purpose in the longer term. BEIS is also engaging with OGDs including DCMS, MHCLG and DEFRA to identify opportunities to bolster the social purpose to reflect wider Government interests in community engagement, loneliness and leveraging community assets. We will need to work with POL to explore how best to link this work to the development of minimum service provision criteria which could range from a minimum service offer for vulnerable customers who require face to face provision, to a local services offer by innovative community branches.

- Exploring the future role of the delivery of government services via POL: BEIS are engaging with a range of OGDs to explore whether we have the right incentives in place for POL to develop both cost effective and customer focused options such as co-location of government services.
- An update on all of these strands will be provided to Ministers in January 2020.
- Government's stated expectation has been for POL to become financially self-sustainable from 2021 (i.e. zero subsidy). The minister has committed to fighting for the continuation of a subsidy to protect the rural network. If payment of a subsidy continues, the company needs to provide a stronger VfM rationale supported by a stronger evidence base.
- Through the long-term vision work BEIS is exploring the possibility of attaching conditions to a post 2021 subsidy to enhance data reporting and improve the transparency of loss-making branches. This will help assess the VfM case for a subsidy in future years.
- As per HMT guidance, POL also needs a mechanism to ensure that this can return to the taxpayer. One option is the provision of a dividend, which we have been pursuing via POL's restructuring project.

## **Change Spend**

### **Lines to Take**

- In our view, the company and Board has been too focused on achieving EBITDAS targets and not sufficiently attentive to change spend and execution.
- Forecasting and monitoring have been weak while some big projects have seen costs over-run and benefits fail to materialise. STIP and LTIP should be redesigned to reward management for managing change spend
- STIP and LTIP should be redesigned to reward cash flow (after change spend) as well as profits.

### **Key messages**

- POL has been insufficiently focused on managing change spend and has continued to have problems with the ways that it is forecasted, authorised and controlled. We asked for greater disclosure and analysis in 2018 and asked for an internal audit to identify the issues with the change spend process and recommend changes. Despite this, problems have continued.
- We have been withholding the remaining £42m of BEIS's allocated investment funding for POL until the business provides a previously agreed rolling 3-year lookahead on investment spend. This has delayed payments that were due in Q1 and Q2 of the financial year. The 3-year lookahead has now been provided and we expect to release the funding by the end of November.
- In future POL will need to reduce its overall need for change spend and improve its efficiency if the company is to be genuinely financially self-sufficient. The current 2018-21 Strategic Plan was intended to be transformational, with only BAU investment required afterwards.
- STIP and LTIP measures have previously focused on EBITDAS. While this encouraged a focus on the company's turnaround, this was at the expense of managing the much larger value in change spend. The use of cash flow metrics would mitigate this problem significantly. This has been discussed at Remco and we are waiting for new proposals from the company.
- The company has recently appointed Dan Zinner as a new Chief Transformation Officer who has been leading a major reorganisation of the approval and monitoring processes, and a reassessment of the portfolio to try to spend smarter and improve the benefit generation from the spending. This has led to POL underspending against targets in this financial year, which in the short term is probably a good sign.
- While we are hopeful that Dan's new approach will lead to improvements, we are considering whether to seek external assurance of their processes in advance of approving a new investment programme as part of the 5 Year Plan.

### **Additional background**

- The need for a greater focus on investment spend was highlighted in the Chair's letter (Annex B)

## **Board and Management**

### **Lines to Take**

- Ask for Tim's views on management changes that Nick Read has made and may choose to make in future, including Al Cameron

### **Key messages**

- Nick Read has replaced the Head of Communications and there may be further restructuring of the senior leadership.
- Al Cameron has returned to his role as Chief Finance and Operations Officer (CFOO) following Nick's appointment. He is eligible for a retention payment if he remains until March 2020. While he has been supporting Nick well to date, we do not know if he will choose to stay
- We have not been impressed by POL's succession planning and this should be an ongoing priority. POL need to think through the interim and transition arrangements in case Al leaves.
- UKGI have pushed POL in the past to create a Strategy function in the business to improve its big-picture thinking when entering in commercial negotiations and avoiding silos. Nick has expressed initial support for this idea and we should reinforce this.

### **Additional background**

- POL's senior leadership team has been in a period of significant and sustained transition. 2019 has seen the departure of the Chief Executive, General Counsel, Chief Information Officer and HR Director. Nick Read has also moved to replace the Head of Communications and there may be further restructuring of the leadership team and a significant number of senior hires, most likely externally.
- Two new NEDs are going on the Board to replace Shirine Khoury-Haq (now CFO at Co-op and therefore conflicted) and Tim Franklin (leaving after his second term expires). Tim will remain Chairman of Post Office Insurance.