



## POST OFFICE LIMITED BOARD REPORT

<b>Title:</b>	GLO separation solution: Managing Issues Arising from GLO Related Matters & Project Starling	<b>Meeting Date:</b>	28 July 2020
<b>Author:</b>	Mark Underwood: LCG Operations Director	<b>Sponsor:</b>	Ben Foat: Group General Counsel

Input Sought: The Board is asked to:

- **Approve**, in principle, an internal restructure / ring-fencing whereby a new 'Historical Matters' business unit including a historical Group executive within the existing Post Office Group, reporting into the existing Post Office Board, noting this does not prevent a new separate entity being formed in due course.
- **Approve** the development of an implementation plan which is to be brought back to Board in September.

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### Previous Governance Oversight

- Pre-Meetings with UKGI 10 June & 30 June, and BEIS 30 June 2020.
- PGLO SteerCo 8 July 2020.
- Post Office Group Executive Meeting of 15 July 2020.

### Executive Summary

1. Although addressing the issues caused as a result of historical practices is important and necessary for Post Office to reset the relationship with Postmasters; the amount of Executive and Board time these matters consume restricts the focus required to ensure Post Office realises its forward looking strategy. The intensity of these matters will also likely increase over the next 12 – 24 months.
2. [REDACTED] Post Office has advised UKGI, BEIS and HMT that Post Office will not be able to fund the potential financial exposure associated with these matters. Post Office will need support from Government. Talks to agree the appropriate mechanism and quantum, have begun and need to continue regularly to ensure these are not overlooked particularly in the 3 year funding round which we understand begins formally in September.
3. In terms of managing the matters which give rise to historical issues and liabilities going forward, Post Office has 3 options:
  - i. **Do Nothing:** These matters and the programme teams continue to be reported up through the existing Post Office Group Executive and the existing Post Office Board.
  - ii. **Internal Re-structure / Ring-fencing:** A new 'Historical Matters' Group Executive is formed as an additional Business Unit within the existing Post Office Group, reporting into the existing Post Office Board.
  - iii. **Separate Legal Entity:** a new legal entity is created, outside of the current Post Office Group, with a new 'Historical Matters' Group Executive reporting into a new Board.

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4. The recommendation is for Post Office proceed on the basis of option 2. This option is less complicated than forming a new legal entity outside of the group and does not prevent a new separate entity being formed in due course, once some of the current 'unknowns' become known. If the Board approve this recommendation, immediate next steps include funding and resourcing a project team, with support from external legal advisers and consultants. The first deliverable being an implementation plan for the September Board.

### Questions addressed

1. What options exist for Post Office to separate itself from managing historical issues arising from the GLO and Starling?
2. What are the advantages and disadvantages of each option, including the associated timeframes and costs?
3. What is the recommended approach and why?
4. What are the risks of not taking action now?

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### Report

#### **Context**

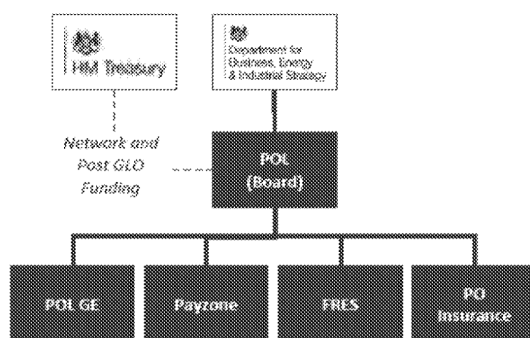
5. This paper and its recommendation has been brought to the Board owing to the following developments / ongoing matters:
  - The recent decision from the CCRC to refer a number of private prosecutions brought by Post Office to the Court of Appeal.
  - The Historical Shortfall Scheme; stood up by Post Office in May 2020, to enable current and former postmasters who were not claimants in the GLO, to make claims for losses relating to historical shortfalls.
  - Post Office's defence of a claim brought by CWU to establish 'worker rights' ("Starling") for a subset of postmasters.
6. The GE and Board receive regular briefings on each of the above matters and will be aware therefore of the significant financial exposure to Post Office, individually and as a collective. The GE and Board are also therefore aware of the amount of time these matters consume at Board and GE Meetings. The level of 'stewardship' these complicated matters also require outside of these meetings from members of the GE, particularly in respect of the Group Chief Executive Officer and Group General Counsel, is significant.
7. Although addressing the issues of the past which gave rise these matters is important and necessary to reset and evolve the relationship with Postmasters, the CEO and the rest of the GE need to be able to focus on delivering a self-sustaining commercial future for the company.

#### **Options**

8. Post Office, UKGI, BEIS and HMT recognise that although Post Office has managed the financial costs of GLO and Starling related matters to date (including the £58m settlement figure agreed in December 2019 with the GLO claimants), should any of the potential financial exposure associated with these matters crystallise, Post Office will need support from Government.

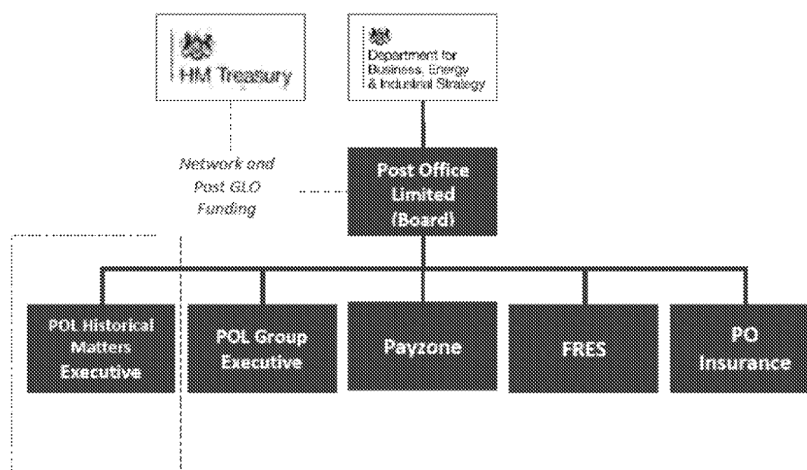


9. Talks to agree the appropriate mechanism and quantum, should begin and continue regularly to ensure these are not overlooked in the 3 year funding round which we understand begins formally in September. Post Office should seek two distinct 'pots' of funding; network funding and funding to manage and provide for the potential liabilities attached to these matters.
10. In terms of the management of these matters going forward, broadly speaking Post Office has 3 options:
  - i. **Do Nothing:** These matters and the programme teams continue to be managed and reported up through the existing Post Office Group Executive and the existing Post Office Board.



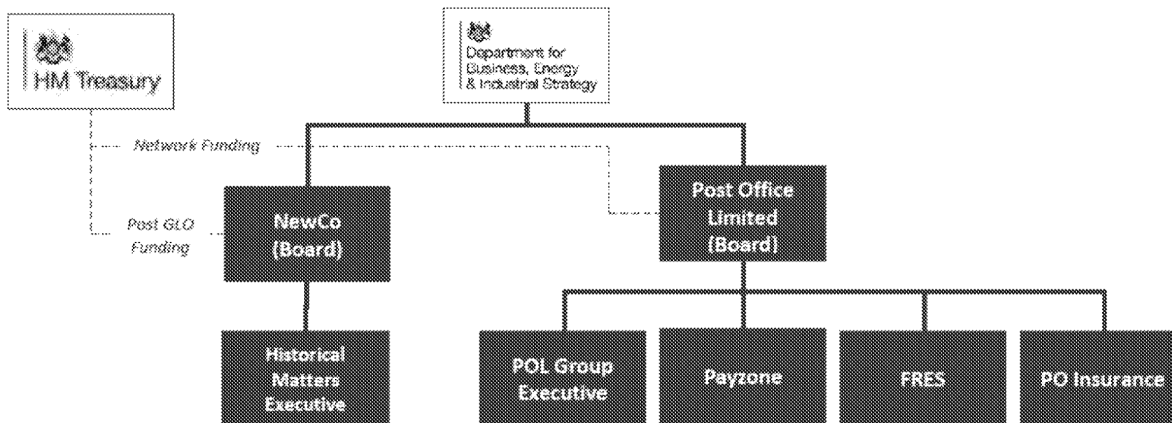
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- ii. **Internal Re-structure / Ring-fencing:** A new 'Historical Matters' Group Executive is formed as an additional Business Unit within the existing Post Office Group, reporting into the existing Post Office Board. A new executive director within that executive committee would be appointed to have accountability for managing this programme of work.





iii. **Separate Legal Entity:** a new legal entity is created, which sits outside of the current Post Office Group, with a new 'Historical Matters' Group Executive reporting into a new Board. The current programme teams move into this new separate legal entity.



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11. Each of the options, along with their respective advantages and disadvantages are set out below. Also included are indicative timeframes and costs.

Considerations	Option 1 Do Nothing / Status Quo	Option 2 Internal Restructure / Ring-fencing <u>inside</u> Post Office Group	Option 3 Create a Separate Legal Entity <u>outside</u> of Post Office Group
<b>Executive Summary</b>			
<b>High Level Advantages</b>	<ul style="list-style-type: none"> <li>No change to the status quo and thus, the simplest of the 3 options, with no lead time, 'set up' costs or broader considerations required.</li> </ul>	<ul style="list-style-type: none"> <li>Existing Post Office Group Executive can focus on delivery the future strategy for Post Office.</li> <li>Simpler and cheaper to execute than creating a separate legal entity <u>outside</u> of the Post Office Group (and does not prevent you from doing so in due course, once some of the current 'unknowns' become known).</li> </ul>	<ul style="list-style-type: none"> <li>Existing Post Office Group Executive and Board can focus on delivery the future strategy for Post Office.</li> <li>Allows for 'true' separation between the management of historical issues and delivery of a new strategy.</li> </ul>
<b>High Level Disadvantages</b>	<ul style="list-style-type: none"> <li>Not believed to be sustainable in the medium to long term.</li> <li>Existing Post Office Group Executive &amp; Board continue to spend a disproportionate amount of time providing oversight and management of these matters.</li> </ul>	<ul style="list-style-type: none"> <li>Existing Post Office Group Executive loses oversight of what is an important matter – the appropriate management of which is required in order to reset the relationship with Postmasters.</li> <li>Challenges regarding establishing clear and transparent separation between Post Office Group Executive and Historical Matters Group Executive.</li> </ul>	<ul style="list-style-type: none"> <li>Existing Post Office Group Executive and Board loses oversight of what is an important matter – the appropriate management of which is required in order to reset the relationship with Postmasters.</li> <li>Complicated and expensive, with a long lead time and dedicated programme team (with external support) required in order to execute.</li> </ul>



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		<ul style="list-style-type: none"> <li>Existing Post Office Board continues to spend a disproportionate amount of time providing oversight and management of these matters.</li> </ul>	
<b>Key Design Principles</b>			
<b>Provides financing for liabilities?</b>	<b>No:</b> requires separate funding mechanism with Government. Post Office is unable to proceed without a separate funding mechanism in place, though Treasury are likely to expect some form of contribution from Post Office.	<b>No:</b> requires separate funding mechanism with Government. Post Office is unable to proceed without a separate funding mechanism in place, though Treasury are likely to expect some form of contribution from Post Office.	<b>No:</b> requires separate funding mechanism with Government. Post Office is unable to proceed without a separate funding mechanism in place, though Treasury are likely to expect some form of contribution from Post Office.
<b>Provides bandwidth for existing Post Office Group Executive?</b>	<b>No:</b> <u>existing</u> Post Office Group Executive will continue to provide oversight of these matters, with Group GC as sponsor.	<b>Yes:</b> a <u>new</u> 'Historical Matters' Group Executive is formed as an additional Business Unit within the <u>existing</u> Post Office Group.	<b>Yes:</b> a <u>new</u> 'Historical Matters' Group Executive is formed <u>outside</u> of the existing Post Office Group.
<b>Provides bandwidth for existing Post Office Board?</b>	<b>No:</b> <u>existing</u> Post Office Group Executive will continue to report up into the <u>existing</u> Post Office Board.	<b>No:</b> a <u>new</u> 'Historical Matters' Group Executive will report into the <u>existing</u> Post Office Board.	<p><b>Yes:</b> a <u>new</u> 'Historical Matters' Group Executive will report into a <u>new</u> Board <u>outside</u> of the Post Office Group.</p> <p><u>However Post Office Board will retain responsibility for liability. To the extent any decision making authority is being delegated/transferred to an external entity it must therefore (through claims management and other governance agreements) satisfy itself that it complies with its director's duties.</u></p> <p><u>Any claims management / governance agreements between POL and NewCo will therefore careful consideration.</u></p>
<b>Other considerations</b>			
<b>Funding for litigation and claims liability</b>	<ul style="list-style-type: none"> <li>POL to be funded directly by HMT / BEIS in respect of i) Network funding; and ii) Litigation / claims liability funding.</li> </ul>	<ul style="list-style-type: none"> <li>POL to be funded directly by HMT / BEIS in respect of i) Network funding; and ii) Litigation / claims liability funding.</li> </ul>	<ul style="list-style-type: none"> <li>As POL retains liability for claims, funding <u>must</u> still be provided for claims settlement liability.</li> <li>POL to be funded either directly or indirectly by HMT / BEIS. UKGf's current proposal is that HMT / BEIS will fund NewCo<sup>1</sup>, which in turn will indemnify POL.</li> <li><u>If funding is to be provided by NewCo, POL Board must be satisfied that NewCo has ability to satisfy funding obligations, as NewCo will have no significant assets.</u> Therefore, POL Board will need to review and be comfortable with</li> </ul>

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<sup>1</sup> In respect of Litigation / claims liability funding, POL would receive Network funding



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			funding arrangements between NewCo and BEIS as shareholder.
<b>Timing</b>	<ul style="list-style-type: none"> <li>No upfront timing considerations.</li> <li>However, any increased claims management activity would consume even more of existing Post Office Group Executive's time.</li> </ul>	<ul style="list-style-type: none"> <li>Establishment of the litigation management/governance framework as well as additional requirements including, executive recruitment.</li> </ul>	<ul style="list-style-type: none"> <li>Establishment of the litigation management/governance framework as well as additional requirements for establishment of NewCo, including director appointment, executive recruitment and NewCo incorporation/articles of association.</li> <li>Establishment of NewCo should be relatively straightforward and unlikely to cause significant delays, assuming use of shelf company and articles reproduced from POL's existing articles. However, the additional complexity of establishing the governance framework on an arm's length basis will be more time consuming.</li> </ul>
<b>Due diligence requirements</b>	<ul style="list-style-type: none"> <li>No due diligence required</li> </ul>	<ul style="list-style-type: none"> <li>Low / medium level of due diligence required to identify personal and business functions required to establish internal ring-fenced business unit.</li> </ul>	<ul style="list-style-type: none"> <li>High level of due diligence required to identify assets, personal and business functions to transfer to NewCo.</li> <li>Asset, contracts and employee transfer, shared services and change of control due diligence.</li> <li>Market/fair value diligence for sale assets .</li> </ul>
<b>Transaction documentation</b>	<ul style="list-style-type: none"> <li>No transaction documentation required.</li> </ul>	<ul style="list-style-type: none"> <li>No transaction documentation required.</li> </ul>	<ul style="list-style-type: none"> <li>Business Sale Agreement to transfer required assets and business functions to NewCo.</li> </ul>
<b>Organisational structure and Governance</b>	<ul style="list-style-type: none"> <li>No new or additional structural or governance requirements.</li> <li>Existing Post Office Group Executive retains oversight of claims management.</li> </ul>	<ul style="list-style-type: none"> <li>Litigation management/governance framework to be established for ring-fenced business unit.</li> <li><u>New</u> Historical Matters Executive within POL has day-to-day oversight of claims management and reports directly to <u>existing</u> POL board.</li> <li>Re-establishment of Board Subcommittee. Postmaster Representative?</li> </ul>	<ul style="list-style-type: none"> <li>Litigation management/governance framework to be established for NewCo.</li> <li>NewCo Executive has day-to-day oversight of claims management and reports directly to NewCo board.</li> </ul>
<b>Agreements and contracts</b>	<ul style="list-style-type: none"> <li>Funding Agreement with HMT / BEIS for claims/liabilities.</li> <li>No additional agreements or contracts required.</li> </ul>	<ul style="list-style-type: none"> <li>Funding Agreement with HMT/ BEIS for claims/liabilities.</li> <li>Employment contract(s) for any new designated Historical Matters Executive/employees.</li> </ul>	<ul style="list-style-type: none"> <li>Funding Agreement with HMT / BEIS and NewCo for claims/liabilities.</li> <li>Claims management agreement between POL and NewCo.</li> <li>Indemnity agreement between NewCo and POL.</li> <li>Shared Services agreement for any POL shares services required by NewCo.</li> <li>Confidentiality and Data Sharing Agreements for providing information on historic claims to New Co.</li> </ul>



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			<ul style="list-style-type: none"> <li>• Licences, permits and insurances required to operate NewCo as standalone business.</li> <li>• Employment contract(s) for NewCo Executive/employees.</li> <li>• Appointment letters for NewCo Board.</li> <li>• AoA and other constitutional documents.</li> </ul>
<b>Funding for ongoing operations</b>	<ul style="list-style-type: none"> <li>• No additional operational funding required.</li> </ul>	<ul style="list-style-type: none"> <li>• Minor additional ongoing operational funding required to support new business unit, including any new employees or roles required to oversee business unit.</li> </ul>	<ul style="list-style-type: none"> <li>• Higher additional ongoing operation funding required to support NewCo as a standalone business.</li> <li>• Funding of NewCo either to come directly from HMT /BEIS or through payment from POL for litigation management services.</li> </ul>
<b>Tax</b>	<ul style="list-style-type: none"> <li>• No additional tax considerations.</li> </ul>	<ul style="list-style-type: none"> <li>• No additional tax considerations.</li> </ul>	<ul style="list-style-type: none"> <li>• Tax analysis required for transfer of business and ongoing relationship between POL and NewCo.</li> <li>• NewCo will require separate tax advice</li> </ul>
<b>Regulatory</b>	<ul style="list-style-type: none"> <li>• No additional regulatory considerations.</li> </ul>	<ul style="list-style-type: none"> <li>• No additional regulatory considerations.</li> </ul>	<ul style="list-style-type: none"> <li>• Analysis required to determine whether NewCo is undertaking a regulated activity as a 'Claims Management Company'.</li> </ul>
<b>People and pensions</b>	<ul style="list-style-type: none"> <li>• No additional employment or pensions considerations.</li> </ul>	<ul style="list-style-type: none"> <li>• New business unit to be made up of existing POL employees.</li> <li>• Employment/appointment of new Historical Matters Executive.</li> <li>• No additional pensions considerations.</li> <li>• Who will transfer</li> <li>• Knowledge transfer / culture - How to leverage information / learnings to ensure that POL retains the lessons learnt from GLO and continues to embrace additional learnings and its new culture of transparency and fairness.</li> </ul>	<ul style="list-style-type: none"> <li>• Appointment of NewCo Board – who will appoint directors? Will these be the current POL directors or a new board appointed by BEIS (as it is outside of POL Group)?</li> <li>• NewCo to employ new and existing POL employees – TUPE considerations.</li> <li>• Employment/appointment of NewCo Executive.</li> <li>• Pensions considerations for transferring employees.</li> <li>• Who will transfer</li> <li>• Knowledge transfer / culture - How to leverage information / learnings to ensure that POL retains the lessons learnt from GLO and continues to embrace additional learnings and its new culture of transparency and fairness.</li> </ul>
<b>Indicative timeframes and cost</b>	<ul style="list-style-type: none"> <li>• No additional costs</li> </ul>	<ul style="list-style-type: none"> <li>• Timing 3-6months</li> <li>• Legal fees: c£100k</li> <li>• Programme Team: c£240k</li> <li>• Consultancy firm: c£180k</li> <li>• Search, appointment and remuneration of members of the 'Historical Matters Group executive: tbc</li> </ul>	<ul style="list-style-type: none"> <li>• Timing 6-12months</li> <li>• Legal fees: c£210k</li> <li>• Programme Team: c£480k</li> <li>• Consultancy firm: c£180k</li> <li>• Search, appointment and remuneration of members of the 'Historical Matters Group executive and NewCo Board: tbc</li> </ul>

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		<ul style="list-style-type: none"> <li>Total: &gt;£540k + ongoing costs (e.g. remuneration of Exec)</li> </ul>	<ul style="list-style-type: none"> <li>Total: &gt;£890k + ongoing costs (e.g. remuneration of Exec)</li> </ul>

12. The level of cost, complexity and disruption increases as you move from option 1 to option 3. This is to be balanced against the level of genuine separation achieved. 'Doing nothing' risks Post Office being unable to realise its forward looking strategy and failing to become a self-sufficient, commercially sustainable organisation - particularly as the workload and subsequent required level of 'stewardship' from the Group Executive and Board will likely increase over the next 12-24 months.
13. Given the current unknowns<sup>2</sup> and the associated cost, complexity and timeframes associated with the remaining options – the recommendation is that Post Office proceed on the basis of option 2 - A new 'Historical Matters' Group Executive is formed as an additional Business Unit within the existing Post Office Group, reporting into the existing Post Office Board.

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**Next Steps**

14. If the Board approve the recommendation, a project team will be resourced and stood up, supported by external legal advisers and a consultancy firm. The immediate deliverable, for the September Board, will be a comprehensive implementation timeline and plan which will include the considerations set out in the earlier table. This requires funding.
15. A letter should be sent to UKGI and BEIS setting out the concept and implementation plan.
16. KPMG and Linklaters are well placed to support Post Office with delivery owing to their involvement on Project Legal Entity Optimisation (LEO). Their support is required owing to a lack of bandwidth and experience in executing these types of matters within Post Office. KPMG would be a non-compliant direct award and procurement risk exception notice will be included within the separate Procurement Board Paper.

<sup>2</sup>e.g. the merits of claims brought through the historical Shortfall Scheme; the number of referrals which will be made to the Court of Appeal; whether any historical convictions will be overturned and claims for malicious prosecution brought; whether the October Starling Tribunal will proceed in October and whether the claimants will actually establish worker status.