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Date: XX May 2018
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Recipient	To Note / Comment	To Approve / Decide
Permanent Secretary	X	

POST OFFICE – LITIGATION RE HORIZON IT SYSTEM

Summary

1. To notify and update you about the potentially high-profile civil litigation brought against Post Office Limited (POL) in relation to the Horizon IT system. We are liaising with POL to ensure that you, the Department and UKGI have sufficient oversight while protecting POL’s legal privilege in its defence against the litigation.

Timing

2. Routine. This is not a new issue but an update is timely as we approach the first hearings in November this year. UKGI is developing an information sharing protocol with POL that seeks to balance oversight requirements with POL’s legal privilege concerns. We will submit the protocol for your approval in due course.

Recommendations

3. That you note the issues, risks and next steps set out below.

Advice

4. Paragraphs 5 to 22 below represent POL’s description of the background to the litigation, the nature of the complaint to be considered by the courts, the litigation process and measures – both past and ongoing – taken by POL. Paragraphs 23 to 27 below represent UKGI’s description of HMG oversight to date and UKGI’s analysis of the impact of this case on POL.

Background to the litigation – provided by POL

5. Transactions at the post office counter are undertaken on the Horizon system, which is used by c50,000 people per day across the network, and which POL estimates has been used by around half a million employees, agents or employees of agents since it was introduced in 1999.
6. In 2012, a small number of (mostly former) subpostmasters, under the banner of the “Justice for Subpostmasters Alliance” (“JFSA”) and with support from some MPs led by then-MP (now Lord) James Arbuthnot, claimed POL’s Horizon IT system had caused losses (shortfalls in physical cash against cash holdings recorded on Horizon) which they had had to make good. In some cases they had been prosecuted for these losses (usually for false accounting, theft or both) while, in other cases, they claim that it led to financial hardship, bankruptcy or consequential, personal losses ranging from divorce to suicide.

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7. An independent firm of forensic accountants, Second Sight, were commissioned to examine the system for evidence of flaws which could cause accounting discrepancies. Second Sight's initial report in June 2013 found no evidence of systemic flaws in Horizon. A final report in 2015 did find that in some cases POL could have provided more training and support to some subpostmasters, though Post Office disputes many of Second Sight's findings.
8. A complaint review and mediation scheme ("the scheme") was established in 2013, with JFSA involvement, to work through 150 applications in an effort to understand and ideally resolve the individual disputes. This included specific investigation into each of the 136 individual cases accepted into the scheme (the other 14 having been capable of summary resolution). As before, no evidence of systemic flaws in the system was found; rather the investigations (by Second Sight and Post Office) found that the main reason for losses in the majority of cases was "errors made at the counter" by the subpostmaster or their staff. To date, UKGI and BEIS have not been privy to the details of individual cases, as POL considers these to be confidential between POL and the individuals.
9. The scheme was closed in early 2015 once all 136 applicants had received reports from POL and Second Sight into their individual complaints. The JFSA however was not satisfied with the outcomes from the scheme, with many applicants seeking substantial sums in compensation which were not forthcoming, and others seeking to overturn criminal convictions which the scheme could never provide.
10. None of the scheme applicants convicted of an offence have appealed their conviction or their sentence.¹ However, since the scheme launched, 33 individuals with convictions have applied to the Criminal Cases Review Commission (CCRC), whose review process has now been going on for around three years. BEIS/UKGI have disclosed information to the CCRC, as required to do by law, for their investigations, as has POL. POL does not know when the CCRC will reach a decision in any of the cases.
11. There has been significant lobbying by the JFSA of Parliament and through the media, although this has not altered POL's position which is that these are individual disputes which are now best resolved through the Court's processes.

Nature of the current complaint to be considered by the courts – provided by POL

12. In recent years, the focus of the complaints by subpostmasters has shifted from issues with the IT system, to the alleged "unfairness" of the contract between POL

¹. On 14 August 2017 Post Office did however receive notice from the Criminal Appeal Office that a former subpostmaster is seeking permission to appeal his 25 September 2008 conviction on 11 counts of theft following losses of £208,000 at the Post Office branch where he had been subpostmaster. The appellant did not apply to the scheme or to the CCRC, and is not a Claimant in the Post Office Group Litigation. This matter currently rests with the Court for a decision.

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and subpostmasters. These allegations are now being progressed in the High Court "Post Office Group Litigation".²

13. The litigants are claiming that their written contract did not reflect the true nature of the POL–subpostmaster relationship. While they accept that there was a principal–agent relationship in force, they nevertheless maintain that the relationship was a closer one akin to an employment relationship and, as such, they are trying to shift the burden of responsibility for explaining accounting losses from subpostmasters to POL. Linked to this, they are also seeking to establish that the contract implies other terms that further shift the burden of responsibility onto POL – for example, that POL had an obligation to provide sufficient training to Subpostmasters to help them avoid accounting errors.
14. There are now around 561 Claimants in the case. The common features of the Claimants are that most were engaged on Post Office's standard contract terms and all will have used the Horizon system. Post Office denies that the contracts should be interpreted as contended by the Claimants, and also contends that many Claimants do not have standing to bring claims because they are time-barred, an abuse of process due to pre-existing criminal convictions, or have already been resolved, with signed settlement agreements in place.

The Litigation Process – provided by POL

15. Post Office has engaged two QCs and are being advised by Womble Bond Dickinson, a major transatlantic law firm.
16. The claim was served on Post Office on 5 August 2016. Several procedural hearings have been held since then. The first substantive hearing ("Common Issues Trial") will commence on 5 November 2018 for four weeks. The Common Issues Trial will principally look to determine the true meaning and effect of Post Office's standard contracts. Six Lead Claimants have been selected to assist with this. The "Horizon Issues Trial" will then be held in March 2019 to look in detail at the specific technical issues claimed in relation to Horizon, which will be determined with the assistance of expert evidence. Further trials will then be needed to resolve other issues, including whether Post Office has breached any of its obligations, and if so, the damage caused by such breach.
17. The nature of the claims include claims for loss of future earnings, other business losses, reputational damage and emotional harm. Although some Claimants have provided some indicative claim values, these are incomplete, inconsistent, possibly duplicative and prone to inaccuracy, and Post Office has raised its concerns in this regard with the Court. The Claimants have not yet formally articulated the quantum of their aggregate claims and Post Office does not expect that they will do so until after judgment is received on the Common Issues trial, later in November/December 2018.

² *Bates & Others v. Post Office Limited*, High Court of Justice, Queen's Bench Division, Claim No's HQ16X01238, HQ17X02637, HQ17X04248.

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18. To date, there have been no settlement discussions between the parties. The Court has ordered the parties to attend mediation after receipt of the judgment on the Common Issues Trial.
19. POL is currently seeking security for its costs, such that they have assurance that should they win the case they can seek to recover costs from the Claimants. Both parties have filed cost budgets with the Court, with the estimated litigation costs for each side up to the end of the Horizon Issues Trial being in the region of £13m (inclusive of all costs incurred to date).
20. The Claimants' action is being funded by a private equity firm, Therium, who specialise in legal claims. If this follows a traditional litigation funding model, Therium will take a cut of any compensation awarded to the Claimants. The specific funding arrangements in place for this litigation are however privileged to the Claimants, and therefore not available to POL at this stage of the proceedings.

Previous measures and ongoing measures taken by POL – provided by POL

21. POL considers that it has undertaken a significant amount of work ever since the claims were first raised to establish the nature of the issues raised by the subpostmasters. In addition to the scheme, which was entirely funded by POL, and paying for the Second Sight forensic investigation (whilst also reinvestigating each case itself), POL has taken and continues to take privileged legal advice from Leading Counsel and engaged Dr Robert Worden of Charteris Consulting Ltd as its experienced expert IT witness. This advice is being kept under continuous review by POL's senior management.
22. POL has established a board sub-committee to consider the issues as they arise on behalf of the board. The schedule for both the sub-committee meetings and board meetings has been synchronised to the Group Litigation Timetable so that POL and its advisors can provide regular updates at critical junctures in the trial process.

HMG oversight to date – UKGI's description

23. This is not the first briefing on this matter. UKGI has been communicating with POL to understand how the various investigations, mediations and legal cases have been progressing. However, UKGI has not been involved in the details of individual cases, nor can we assess or manage the legal or operational risks attached to it, which is for POL to do. To date:
- UKGI has provided several briefings to Ministers, as well as day one briefings.
 - At our request, The Post Office Chair and CEO have also briefed Ministers in the past and would be happy to do so again.
 - As part of his role on the Board, shareholder representative Richard Callard sat on the Board sub-committee on this matter, until this was disbanded after the mediation scheme ended in 2015. A new sub-committee has now been established as the case approaches, upon which the new shareholder representative director Tom Cooper sits.

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- ShEx/UKGI assisted the CCRC in its enquiries, disclosing files held by BIS.
 - BEIS Legal have been kept updated and held discussions with POL shortly after the last case management meeting (more details below).
24. Since the High Court proceedings for the civil litigation were issued in April 2016, the issue has been much quieter as we awaited further details and likely direction of the case, which are only now emerging. We have briefed Andrew Griffiths in person, and his office have an action to arrange a meeting with POL's General Counsel, so that the Minister may be directly appraised with respect to the progress and risks attached to this case, and you may wish to attend.
25. UKGI considers that the case is potentially significant in light of:
- (a) The presentational dynamics of a long-running and in some cases, bitter, dispute between small sub-postmasters and POL;
 - (b) the threat to the agency relationship which is key to the POL business model;
 - (c) the breadth and nature of the legal arguments that could arise, some of which touch upon policy areas in the BEIS portfolio - for example, we are aware of another group of sub-postmasters seeking to characterise the relationship as an employment relationship (in an UBER type case). Another potential tangent would be to characterise small subpostmasters as akin to consumers, requiring protection from overtly punitive or unfair contractual terms.

Impact on POL and mitigation – UKGI's view

26. In addition to the significant cost and level of management attention this dispute has entailed for POL over the last few years, UKGI believes that impacts include the following:
- POL has been less rigorous in its enforcement of its contract when money goes missing. With a network of over 11500 branches it is inevitable that some individuals working in the network, including subpostmasters, are less honest or competent than the vast majority. POL has still suspended or terminated the contracts of subpostmasters where they have been found to be at fault, but has been less rigorous in its recovery of funds, focussing instead on trying to spot discrepancies as they emerge and limit their size. POL is seeing the effect of this, in that there appears to be an uptick in issues of fraud (and of those accused of fraud joining the litigation proceedings, making recovery harder).
 - POL has had to take greater care in the roll-out of its new Horizon equipment than would otherwise be the case, making a complex implementation all the more complicated.
 - Given the shift in the claimant's argument from the IT system to the "unfairness" of the contract, they may also seek to link into the broader debate about lack of employment or consumer protections for contractors. POL itself periodically faces separate cases whereby subpostmasters claim that their

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status is that of an employee or a worker rather than an agent – POL was notified on 25 April that 120 subpostmasters have launched such a claim - and these could further complicate the Horizon litigation (or vice versa). Given that the majority of post office branches are run by self-employed subpostmasters on an agency basis, an adverse ruling could force POL to reformulate contracts for new operators and renegotiate existing contracts, and, by extension, potentially impact more broadly on its operating model and commercial sustainability.

- As explained by POL in paragraph 17 above, claimants have not yet formally articulated the quantum of their aggregate claims and POL does not expect this to happen until after judgment is received on the Common Issues trial in November/December, so it is difficult for UKGI to assess the financial liability with any degree of accuracy. However, from previous discussions with POL about their experience of the mediation scheme and their bilateral discussions with subpostmasters before this case started, our best estimate at this stage for the high-water mark for the quantum of the claims against POL is c£250m, though this may include claims for loss of future earnings, school fees, reputational damage etc, for which POL may not be liable even if the court found against POL.
27. In terms of mitigating against legal and operational risks, POL has summarised its past and ongoing measures in paragraphs 21 and 22 above. In addition to these, UKGI is aware from past discussions with POL that POL did the following:
- appointed Deloitte in 2013 to look at the Horizon system to establish its veracity. Whilst this was a limited study due to the passage of time, at that time POL informed us that no issues were found.
 - at Baroness Neville-Rolfe's request, when she was the responsible BIS Minister, the then incoming POL Chair Tim Parker commissioned a new QC to investigate the matter when he joined POL in October 2015. The initial findings satisfied the Chair that POL had taken the appropriate action at each stage. With the announcement of the group litigation in November 2015, the Chair decided following legal advice not to conclude the investigation on the grounds that it could have impacted the Court's consideration of the claims.
 - POL has also investigated individual cases and at the time informed us that no systemic issues were found.

Communications Advice (agreed with BEIS Comms)

28. The JFSA has generated considerable coverage on this issue in the past, including The Daily Mail, The One Show, Panorama and parliamentary debates. If this court case proceeds, we will refer any media to POL and state that this is a matter for POL and the courts and that it would be inappropriate for Government to comment. If the court case is dropped, we would give media a line stating that we respect the judgment of the courts and refer back to the independent investigations by Second Sight and Deloitte that found no evidence of flaws in the Horizon IT system.

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Contributors (*Retain the relevant sentence and identify who has provided input*)

29. This advice does not have financial considerations, as agreed with Syed Magrhabi. Financial advice will be provided once a better quantification of the claim can be established.
30. Legal (Gareth Evans) and UKGI legal have been consulted and agreed the content of this advice.
31. Communications considerations have been taken into account, and agreed with Jessica Shepherd and Chris Swoffer.
32. Parliamentary handling has been taken into account, and agreed with Richard Callard. As noted above, this issue flares up periodically, but whilst the case remains with the courts Parliament it is less likely that the issue will be considered in Parliament.