



Sarah Munby
Permanent Secretary & Principal Accounting Officer
Department for Business, Energy & Industrial Strategy
1 Victoria Street
London
SW1H

5th August 2021

Dear Sarah,

For Approval: Post Office Incentive Schemes for the Chief Executive Officer and Chief Finance Officer

I am writing to request approval to include the Chief Executive Officer (CEO) and Chief Finance Officer (CFO) of Post Office Limited in the Short-term Incentive Scheme (STIP) for 2021/22 and the Long-term Incentive Scheme (LTIP) for FY 2021/24.

I am also writing to request approval for an adjustment to the EBITDAS target within the LTIP for 2019/22. As set out in the Articles of Association of POL (Articles 50 to 52), the remuneration of all Board members including the CEO and CFO requires approval by the Shareholder.

The STIP and LTIP were approved by the Remuneration Committee in July 2021 in respect of the Group Executive (GE) and Senior Leadership group (SLP). At the same time, the Remuneration Committee approved the adjustment of the EBITDAS target within the LTIP for 2019/22.

The proposals requiring your approval in relation to the CEO and CFO are:

1. To include the CEO and CFO in the STIP for 2021/22
2. To include the CEO and CFO in the LTIP for 2021/24
3. To adjust the EBITDAS target within the LTIP for 2019/22

1. 2021/22 STIP

The CEO and CFO are eligible to participate in a STIP as follows:

Position	Threshold	On-target	Stretch
CEO	24%	30%	45%
CFO	32%	40%	66%

Payments under the plan are determined in line with the achievement of performance criteria, as follows:

Gateway measure		
Measure	Detail	Target
Network coverage	Maintain branch network	11,500 branches are maintained <i>(subject to any waiver)</i>

There are Company measures in the plan which account for 80% of the plan payment and comprise both financial and Postmaster-centric measures. The remaining 20% is on personal performance in line with the rating received through the Performance Management process.

The financial and Postmaster-centric measures are weighted 40/60 and the targets are as follows:

Weighting	Measure	Detail	Threshold	Target	Maximum
40%	EBITDAS	As per agreed definition	£41.6m <i>(80% of Board agreed target)</i>	£52m* <i>(100% of Board agreed target)</i>	£62.4m <i>(120% of Board agreed target)</i>

Postmaster centric measures					
Weighting	Measure	Detail	Threshold	Target	Maximum
60%	1) Postmaster satisfaction (15%)	Measured by question B1 and B7 (baseline 17% and 25% respectively)	30%	33%	36%
	2) Transaction corrections (15%)	Aged transition items average (baseline average 1,647)	1,400	1,200	1,000
	3) Growth in total revenue on 2 core product areas (financials not volume)	Mails	£331m (90% of target)	£368m (2019/20 new commercial s from MDA 2)	£405m (110% of target)
		(Mails 7.5% Banking 7.5%)	Banking	£190m (90% of budget)	£214m (100% of budget)
	4) Improvement in a key area of compliance (Inland 7.5% International 7.5%)	Dangerous goods	Inland 60% International 75%	Inland 70% International 85%	Inland 80% International 95%

Summary of consolidated weighting

Measure	
Individual	20%
Company - financial	32%
Company - Postmaster centric	48%
Total	100%

Detailed information on the measures can be found in Appendix 1

2. 2021-2024 LTIP

The CEO and CFO are eligible to participate in a LTIP as follows:

Position	Threshold	On-target	Stretch
CEO	24%	30%	43%
CFO	40%	50%	70%

As with the STIP, the measures for the LTIP have been mapped against the strategic intent, 7 pillars and 6 priorities. Substantial work has been done, in consultation with the Remuneration Committee, over the course of 2021 to identify what measures would be truly transformational and also clearly sign-post the cultural journey required.

As a result, the following measures and metrics were approved in July by the Remuneration Committee in respect of the GE and SLP population:

Gateway measures (to be achieved before any payment is awarded)		
Measure	Detail	Target
EBITDAS less change spend	Affordability gateway	Achievement of positive EBITDAS less change spend for FY 2023/24. (Note that if change spend is delayed, deferred or aborted a rationale for the deferral or cancellation of the project must be provided in summary to the Committee (with detail available if required) when out-turn for the LTIP is measured and the out-turn and/or target will be adjusted if appropriate).
Network coverage	Maintain branch network	11,500 branches are maintained (<i>subject to any waiver</i>)

Financial measure					
Weighting	Measure	Detail	Threshold	Target	Maximum
40%	Cash flow	Trading profit plus network subsidy payment less interest, less tax, plus investment funding less change spent (excl. HMBU settlement costs) plus movement in net funding position	80% of Board agreed target	100% of Board agreed target	120% of Board agreed target

Non-financial measures – strategic and transformational					
Weighting	Measure	Detail	Threshold	Target	Maximum
60%	Postmaster Promise (15%)	Question B1 and B7 from the Quadrangle survey Discretion can apply if all the year one, two and three actions identified in the five-year Postmaster engagement plan have been completed.	45%	50%	60%
	Systems implementation: delivery (15%)	Number of branches offering full RMG services without Horizon by 31 March 2024	Outstanding branches represent less than 25% of estate and have an implementation date in the next 3-6 months	50% of branches completed by end of 2024	100% of branches completed by end of 2024
	Systems implementation: Postmaster adoption (15%)	Percentage of Postmasters fully adopting/utilising the processes and services available through the new system	70%	80%	90%
	Customer and colleague promises (15%)	The customer and colleague promise measured through progress against: <ul style="list-style-type: none"> customer NPS – (appropriate customer NPS measure to be developed and agreed by 31/12/2021) colleague engagement/NPS to support customer and postmaster promises: (to be developed and agreed by 31/12/2021) Threshold, Target and Maximum to be confirmed			

Please note that there is no individual measure for the LTIP.

Detailed information about the LTIP measures can be found in Appendix 2.

Consideration of progress against recommendations of the Inquiry

In determining the outcome of the LTIP, the Remuneration Committee will take into account the recommendations of the Inquiry when available and review the progress of the Executive against those recommendations. This will also apply to recommendations for the CEO and CFO.

If not available during the LTIP measurement period this measure will be deferred and included in the 2022-25 LTIP and not this 2021-24 LTIP.

3. LTIP 2019–2022: Change in Performance Metric - EBITDAS target

In December 2019, the Remuneration Committee agreed a resolution to “approve the FY2019/22 target and range, based on the 21/22 EBITDAS being £110m with 85% being the threshold figure and 115% being stretch. If business plans change by more than 10% either way, we will replace with the 5 year Plan (5YP) number in March 2020”

In the event the 5YP numbers were not agreed due to Covid-19. The EBITDAS 21/22 target figure was discussed during the additional Remuneration Committee meeting on 9 April 2021, and it was noted that the next step was for the Board to agree the 2021/22 budget and seek approval from the Remuneration Committee to apply this target to the 2019-22 LTIP.

The matter was discussed at the July Remuneration Committee meeting, and it was agreed to align the LTIP EBITDAS performance target for FY21/22 with the Annual Plan figure of £52m. On this basis, LTIP threshold would be £44.2m (85% of target) and stretch would be £59.8m (115% of target).

In reaching this agreement, the Remuneration Committee took into account the significant challenges faced by senior leaders including the impact and on-going effects of the Covid-19 pandemic, the on-going impact of the Inquiry, the negativity associated with the Post Office brand and a significant fall in trading profit during 2020-21.

As the business targets for FY21/22 are expected to change by more than 10% of the original forecast, and in line with the resolution passed by the Committee in December 2019, the Remuneration Committee approved the proposal to make an adjustment to the EBITDAS performance target for FY21/22 in relation to the LTIP. This will align it with the Annual Plan figure of £52m and, whilst it contains a significant amount of stretch, provides a more realistic incentive target.

Correspondingly, we are seeking approval to apply this change to the LTIP 2019 – 22 for the CEO and CFO. This will bring arrangements for the CEO and CFO in line with the other GE members, and also align it with the agreed business targets.

As commented in the STIP section, there is still volatility in the market, and should the EBITDAS target be revised as part of the mid-year Board sessions or earlier, the Remuneration Committee will be asked to consider the new EBITDAS quantum which would follow the 85 – 115% performance range. We will seek approval to apply any revised targets agreed as a result of this review to the CEO and CFO.

In conclusion

I look forward to receiving your approval for the CEO and CFO participation in the 2021/22 STIP and the 2021 – 24 LTIP, together with approval for a change to the EBITDAS target in the 2019 – 22 LTIP.

Yours sincerely

A rectangular box with a dashed border containing the letters "GRO" in a large, bold, black sans-serif font.

Ken McCall

Chair, Remuneration Committee

Appendix 1**Detail of STIP measures*****Financial measure – EBITDAS***

A single financial measure has been proposed in line with the principle that the STIP is simple and easy to understand by all and equally reflects Post Office's mission: a commercial business with a social purpose.

In setting the targets, the principle that has been applied is that the On-target amount is equal to the Board agreed target for 2021/2, with a performance range of 80% to 120% for Threshold and Maximum.

As presented at the Board, it is acknowledged that there is still volatility in the market. The Board have agreed that two stretch assumptions in relation to FRES (£6m) and Labels (£8m) would be tracked through the first half of the year, and baseline targets adjusted downwards accordingly, should these revenues not transpire. This would happen as part of the mid-year Board sessions or earlier. Should the EBITDAS target be revised, the Remuneration Committee will be asked to note the new EBITDAS quantum which would follow the 80-120% spread. In this instance, we would also ask BEIS to note the new EBITDAS quantum and 80-120% range in relation to the metrics for the CEO and CFO.

Postmaster centric measures***Postmaster satisfaction***

It is proposed to use the same two questions from the Quadrangle survey that are included in the Transformation Incentive Scheme:

- B1 "how would you describe your relationship with Post Office"; and
- B7 "how supported, or not, do you feel from Post Office".

These two questions have been selected to provide cohesion through the two schemes (and they are also proposed for inclusion in the 2021/4 LTIP) and provide alignment with the strategic intent and the priorities. The outcome of the Transformation Incentive Scheme will be calculated in January 2022, with the outcome of the 2021/2 STIP around 3 months later. The proposed target of 33% satisfaction for this measure is considered to be very stretching. The baseline (from the January 2021 Postmaster survey) was 17% for question B1 and 25% for question B7. For the Transformation Incentive scheme, the target is set at 30% for both, which means that the target in the STIP represents a 10% improvement in the 3-months from January to April 2022.

Assessment of this measure will be the average result across the two questions.

As with the Transformation Incentive Scheme, it is proposed that the Committee may consider and exercise discretion if all of the actions identified for in-year delivery in the five-year Postmaster engagement plan have been completed.

Transaction Corrections

Assessment of this measure will be on a straight-line basis.

Growth in Mails and Banking

Mails: There has been substantial volatility in the run rate of parcel volumes vs 2019 over the last 14 weeks but this now seems to have settled in a range of +3% to -10%. All indicators are showing ecommerce is now in negative growth.

Analysis suggests that parcel volumes this year will stabilise at -3% vs 2019. At this level, with the new commercial arrangement with Royal Mail, this would bring us to £368m which is £22m greater than the 2019 outturn with parcel revenue up 28% vs 2019 and Special delivery up 20%. Therefore, the target is proposed at £368m. Threshold is the 2019/20 revenue as agreed with the Remuneration Committee while stretch is set at the £390m (pre UKGI stretch £38m budget).

- In response to feedback from the Remuneration Committee for, we have adjusted the figures around the £368m target to represent 90% of Target at Threshold and 110% of Target at Stretch, recognising that this takes the Threshold figures below the 2019/20 actual.
- For clarity, if the £52m EBITDAS target is adjusted downwards because of mails performance, there would be no change to the £368m number for the purposes of the revenue growth metric.

Banking: The Remuneration Committee agreed the principle of using 2019/20 as the pre Covid-19 baseline for threshold targets. However, for Banking, BF2, which started in January 2020, has inflated revenue to such an extent that at £130m this threshold number is too low. Therefore, we are proposing a range +/- 10% for the threshold and stretch around the on-target which aligns with Budget. NB. UKGI budget stretch has only been added to Mails and FRES profit share, the Banking budget is the same under both £38m & £52m versions.

Assessment of this measure will be split 50/50 between Mails and Banking, and on a straight-line basis.

Improvement in a key area of compliance

Assessment against this measure will be split 50/50 between Inland and International, and on a straight-line basis.

Appendix 2

Detail of LTIP measures

Financial measure – cash flow

A single financial measure has been proposed with consideration to the principle that the LTIP is simple and easy to understand by all and equally reflects the Post Office mission.

In setting the targets, the principle that has been applied is that the on-target amount is equal to the target for 2023/4 which is anticipated to be agreed after the autumn 2021 spending review. A range of 80% to 120% of this target on a straight-line basis is proposed. This aligns with the principle set for the financial measure in the STIP. This is a change from the 2019/22 LTIP where the range was set at 85% to 115%.

This measure is weighted at 40% of the total LTIP to allow for increased focus to be given to the transformational elements of the LTIP.

Non-financial measures

These are weighted at 60% (15% per individual measure). Each measure could be achieved independently of each other, and a bonus considered for that element in isolation.

Postmaster Promise

The same two questions (B1 and B7) from the Quadrangle survey are for the LTIP as for both the Transformation Incentive Scheme and STIP. Aligning the same measures over the three incentives clearly signals the importance of these two measures and the action plans to support delivery against them whilst also signposting the improvement expected over the period to 2024. Further stretch improvements would be set for future LTIP awards.

Assessment of this measure would be the average result across the two questions.

Systems implementation: two measures – delivery and Postmaster adoption

It is proposed that there are two measures relating to the systems implementation: the first relating to delivery to be measured by the number of branches offering full Royal Mail Group services without Horizon and the second assessed through measuring the percentage of Postmasters fully adopting/utilising the processes and services available through the new system.

Assessment of these two measures will be on a straight-line basis.

Customer and Colleague Promises

Work is currently underway to develop our customer and colleague promises. Customer progress will be measured against a relevant and appropriate customer NPS measure that will be developed and agreed by 31/12/2021.

Colleague engagement is measured through the engagement survey (to be developed from the Engagement drivers). The inclusion of colleague engagement/NPS is vital to ensure the aligned focus of the organisation on supporting both the customer and postmaster promises. We will analyse the engagement drivers to enable us to use the elements of engagement which most strongly drive the Customer experience. These will be developed and agreed by 31/12/2001.

Assessment of this measure will be 50/50 across Customer and Colleague and will be detailed further once the work is finalised.