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From Paul Lam-Po-Tang

Writer's telephone

GRO

To Keith Baines, Post Office Counters Ltd.,
London

Receiving fax number

GRO

Copy to Paul Rich, Post Office Counters Ltd., London

GRO

Draft POCL/BA/ICL Heads of Terms

I attach for your comments a discussion draft of the Non-Binding Heads of Terms among POCL, BA and ICL, together with an index of the documents which have been incorporated in the Heads of Terms. I also attach for your information a copy of the acceptance flowchart sent to me yesterday by Masons.

The Heads of Terms are based on the latest draft of the heads of terms sent to BA on 2nd December, 1998. I have moved the terms of the BA/POCL agreement to a separate document and have not made any changes to that document. You will see that there are a number of issues which POCL should revert on before the Heads of Terms are circulated outside POCL. I would stress that the attached document is for discussion purposes only and that Jeff and I may have further amendments.

Please would you arrange for a copy of the agreed veto grounds for acceptance to be sent to me.

As discussed earlier this week, I will leave it you to circulate the attached document for comment within POCL. I think it would be worthwhile to have a meeting to discuss the Heads of Terms once you and the others have had a chance to review it.

Regards,

GRO

Paul Lam-Po-Tang

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A list of the partners and their professional qualifications is available for inspection at the above address.
The partners are either solicitors or registered foreign lawyers.

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BA/POCL/ICL PathwayIndex to documents incorporated in BA/POCL/ICL Pathway Heads of Terms**General**

1. Letter dated 9th December, 1998 to Rt Hon S. Byers from K. Todd
2. Agreed volume and pricing assumptions from Corbett discussions [POCL TO PROVIDE COPY]
3. Agreed Programme Plan [POCL TO PROVIDE COPY]
4. Letter dated [●] December, 1998 to S. Sweetman from R. Christou regarding Fujitsu guarantee [POCL TO PROVIDE COPY]

Commercial

5. Memorandum of Understanding
6. Letter dated 21st December, 1998 to D. Murphy from K. Baines re £35 million NPV

Acceptance

7. Acceptance paper dated 17th December, 1998 prepared by D. Miller
8. Acceptance flowchart dated [●] December, 1998 prepared by R. McCallough [sent to P. Lam-Po-Tang on 7th January, 1999]
9. Notes to acceptance flowchart (as amended) dated [●] December, 1998 prepared by R. McCallough [see also fax dated 22nd December to R. McCallough from J. Triggs]
10. Agreed veto grounds for acceptance [POCL TO PROVIDE COPY]

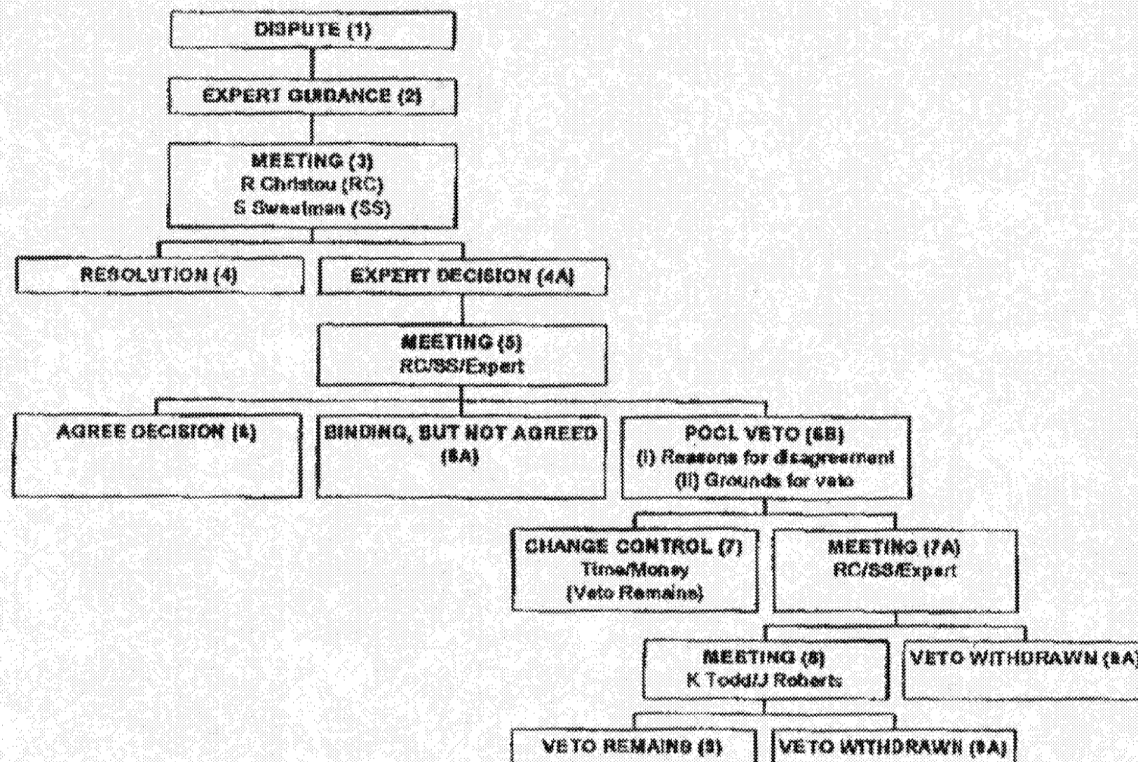
Funding

11. Funding paper dated [●] January, 1999 prepared by ICL [See POCL Funding Paper including revised draft not shown to ICL or BA and see also second ICL Funding Paper]

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ACCEPTANCE DISPUTES - ESCALATION AND RESOLUTION (See attached commentary)



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DISCUSSION DRAFT: JRT/PKYL: 8.1.99

POCL/BA/ICL PATHWAY

*Without Prejudice
Subject to Contract
Strictly Private and Confidential*

Non-Binding Heads of Terms

These draft heads of terms are subject to contract and nothing in this document, save for paragraph M (confidentiality), is intended to create legal relations. Paragraph M is intended to be legally binding.

In due course a binding agreement will include the following aspects and be subject to those conditions set out in Schedule 1 to this document:

A. Contract Extension

1. BA to extend its contract with ICL Pathway so as to expire on 31st March, 2008.
2. POCL to extend its contract with ICL Pathway for banking and potentially other lines of business so as to expire on 31st March, 2010 and such that as from 30th September, 2008, the contract term will continue subject to not less than 18 months termination notice.
3. BA, POCL and ICL Pathway to agree consequential changes to the Authorities Agreement (including the expiry date) to reflect changes to the DSS Agreement and the POCL Agreement.
4. POCL and ICL Pathway to pursue their heads of agreement for future business.
5. BA to aim to migrate all benefit payments business under the Related Agreements as at 31st March, 2005 to ACT over a three year period ending on 31st March 2008 on the basis that 20% of those benefit payments under the Related Agreements will have migrated to ACT by 31st March 2006, 60% by 31st March 2007 and 100% by 31st March 2008.

B. Refresh Costs

To the extent that POCL and ICL Pathway agree that the POCL contract extension requires equipment to be upgraded and replacement equipment acquired, POCL will fund the costs of the upgrade and acquire the replacement equipment itself, on terms satisfactory to POCL. The transfer value on the expiry of the contracts (i) for those assets acquired pursuant to this paragraph will be nil and (ii) for those assets upgraded pursuant to this paragraph will be

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reduced by the value added by the upgrade. Any such upgrades and acquisitions will commence during the contract year 2006/7.

C. Benefit Payment Guarantees

[Before the payment guarantee provisions are agreed, the new acceptance regime will need to be settled.]

1. BA will guarantee the following aggregate payments (the "Benefit Payment Guarantees") for CMS, PAS, BES and OBCS over the Horizon Platform:-

Year	Aggregate Guaranteed Payment
2001/2	£78m
2002/3	£80m
2003/4	£80m
2004/5	£80m
2005/6	£72m
2006/7	£46m
2007/8	£31m

[The above figures are based on the figures which BA provided to KPMG for the purposes of the Corbett proposal.] *[Attach Corbett figures.]*

2. The Benefit Payment Guarantees for BES and OBCS are to be made to POCL and POCL is to give back to back guarantees to ICL Pathway.
3. The amounts for the Benefit Payment Guarantees have been prepared on the basis of actual prices in the relevant year after taking into account any discounts and then multiplying these adjusted prices by the expected volume and by 75%. [The figures also assume that inflation will be less than 6%.]

[BA and POCL to confirm whether guarantees are to increase if inflation is 6% or more.]

4. The Benefit Payment Guarantees are dependent on the system remaining fully functional in accordance with the Related Agreements.

[Specify method of reducing guarantees?]

5. The Benefit Payment Guarantees assume that the programme plan set out in Schedule 5 to this document remains unchanged. BA and POCL may adjust the payment guarantees if the programme plan changes or is not met.

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[How will adjustments be made?]

6. The Benefit Payment Guarantees will commence from the date on which [national rollout of NR2 and [NR2+] has been successfully completed] OR [there is full acceptance of all contracted functionality from Pathway. "Contracted functionality" for this purpose means the full contracted functionality for all BA services under the contracts and the full contracted functionality for all POCL services under the contracts excluding the Logistics Feeder System.]
7. [Once the Benefit Payment Guarantees have commenced, BA will pay guarantees based on each card enabled post office with the contracted functionality to which multi-benefit migration has been completed. If the delay to completion of multi-benefit migration to any individual post office is solely due to the default of BA any of its contractual responsibilities, then BA will pay guarantees for that office as if that delay had not occurred. DSS payment guarantees for an individual post office will be assessed on the basis of the percentage of that post office's business in relation to the UK total of DSS/SSA business. The relevant PIVOT (or replacement) data will be collected for the last available complete year before full acceptance as defined in paragraph C4(ii) above. POCL will make such DSS/SSA data readily available to ICL Pathway and BA and such DSS/SSA data will be available within six months after the relevant year end. Back to back guarantees by POCL for BES and OBCS will also be made on the same basis. Whatever the circumstances the maximum of the guarantees payable in any year will not exceed the sums set out in paragraph C(1) above.]
8. POCL agrees to pay quarterly in advance (as a payment on account of the actual sum due in respect of the relevant quarter) that part of the Benefit Payment Guarantees in respect of BES and OBCS. To the extent that BA does not pay POCL in respect of such Benefit Payment Guarantees, ICL Pathway will reimburse POCL for the amount paid by POCL to ICL Pathway in respect of such unpaid BA amounts.

D. Non-Benefit Payment Guarantees

1. POCL will in addition guarantee the following aggregate payments (the "Non-Benefit Payment Guarantees") for all POCL services, including core business (excluding BES and OBCS), banking business and new products, over the Horizon Platform:-

Year	Aggregate Guaranteed Payment
2001/2	£33.9m
2002/3	£40.5m

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2003/4	£42.1m
2004/5	£40.1m
2005/6	£41.5m
2006/7	£45.6m
2007/8	£54.0m
2008/9	£57.9m
2009/10	£57.0m

2. The amounts for the Non-Benefit Payment Guarantees have been prepared on the basis of actual prices in the relevant year after taking into account any discounts and then multiplying these adjusted prices by the expected volume and by 75%. [The figures also assume that inflation will be less than 6%.]

[POCL to confirm whether guarantees are to increase if inflation is 6% or more.]

3. The Non-Benefit Payment Guarantees are dependent on the system remaining fully functional in accordance with the Related Agreements.

[Specify method of reducing guarantees?]

4. The Non-Benefit Payment Guarantees assume that the programme plan set out in Schedule 5 to this document remains unchanged. POCL may adjust the payment guarantees if the programme plan changes or is not met.

[How will adjustments be made?]

5. The Non-Benefit Payment Guarantees assume that banking services to be provided by ICL Pathway will become available in 2001/2. If this is not the case, then the Non-Benefit Payment Guarantees shall be reduced to reflect the lower volumes that would apply in the absence of banking services.
6. The Non-Benefit Payment Guarantees will commence from the date of acceptance of NR2.
7. The Non-Benefit Payment Guarantees will be reduced by 6% until the contracted APS Smartcard functionality has been released.
8. Once the Non-Benefit Payment Guarantees have commenced, POCL will pay guarantees under paragraph D(1) based on the percentage of post offices which have been automated or would have been automated but for POCL's Default. The Non-Benefit Payment Guarantees will be reduced by a proportion equal to that which the volume of transactions at post offices that have not been

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automated bears to the total volume of transactions at all post offices, in each case as ascertained by reference to the latest PIVOT data for those post offices.

- [9. Until the completion of national rollout of the POCL Infrastructure, the Non-Benefit Guarantee Payments will be calculated as follows:
- (i) For each post office, there shall be calculated the percentage (the "Non-Benefit Percentage") which that post office's annual total non-benefits business (i.e. services other than BES and OBCS) over the Horizon platform represents of the national total annual non-benefits business for all post offices over the Horizon platform for the year ending 31st March, 1999 as recorded on the PIVOT system at the end of that year. For post offices where a full year's data is not available (including, without limitation, because there are new post offices that were not trading at the start of the year) the average value for post offices with the same number of counter positions will be used.
 - (ii) For each calendar month, the monthly extent (the "Monthly Proportion") of completion of roll out of the POCL Infrastructure will be calculated by adding the Non-Benefit Percentages for all post offices at which implementation of non-benefits services shall have been completed before the start of that month. This will be 100% in months after full completion of the roll out of POCL Infrastructure.
 - (iii) For each year ending 31st March, the annual proportion (the "Annual Proportion") of roll out of the POCL Infrastructure will be calculated by adding the Monthly Proportion for each calendar month in that year and dividing by 12. This will be 100% in complete years after full completion of roll out of the POCL Infrastructure.
 - (iv) The Non-Benefit Payment Guarantees that apply in each year ending 31st March after acceptance of NR2 will be calculated by multiplying the Non-Benefit Guaranteed Payment for that year in paragraph D(1) (as adjusted by paragraph D(7)) by the Annual Proportion for that year.]
- [10. If the planned rate of roll out is not achieved solely as a result of POCL contractual default and if POCL shall have failed to mitigate the consequences of such default (including, without limitation, where one post office cannot be automated on the due date because of a POCL contractual default, POCL making another post office with the same volume of business available for automation in its place) then the guarantees will be calculated as if the delay caused by that default had not occurred.]

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11. POCL agrees to pay quarterly in advance (as a payment on account of the actual sum due in respect of the relevant quarter) the Non-Benefit Payment Guarantees.

E. Pricing/Discounts

[POCL and BA agree that the 3 per cent. per annum reduction in prices shall be removed from 1st April 2005 onwards (or an alternative alteration to prices having an equivalent NPV over an equivalent time frame).]

[The new pricing regime will be linked to RPI. Prices will be reduced once a year by an amount equal to $(RPI - [\bullet]\%)$ multiplied by the prices for the previous year.]

Pathway is to grant a discount of 25 per cent. in respect of volumes of POCL non-benefit business transactions exceeding 120 per cent. of the volumes assumed in the Corbett discussions on an aggregated basis.

[Attach Corbett volumes]

F. Contractual Acceptance

The parties agree to amend the Related Agreements in relation to acceptance [(including acceptance specifications)] in accordance with Schedule 2 to this document.

G. Programme Timetable

The contractual milestones will be adjusted in line with the current programme timetable set out in Schedule 5 to this document.

H. Amendments to Contracts to Facilitate Borrowing

The amendments set out in Schedule 3 to this document shall be made to the Related Agreements in order to facilitate ICL Pathway's borrowing.

I. Other Matters *[Running Sores]*

The outstanding issues of contention described in Schedule 4 to this document shall be finally resolved in the manner set out in that schedule.

[BA's overall offer under the Corbett negotiations was based on BA's understanding that all outstanding "running sores" be settled at no additional cost or risk to BA.]

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J. Arrangements between POCL and BA

The agreement between POCL and BA set out in Schedule 7 to this document shall take effect.

K. Ongoing Financial Condition

Fujitsu shall provide to BA and POCL a legally binding and enforceable guarantee of all of ICL Pathway's obligations under the Related Agreements (as amended). This means that, amongst other things, Fujitsu will ensure that those obligations are fulfilled, on and subject to the terms of the Related Agreements, notwithstanding any insolvency of ICL Pathway.

The guarantee will be governed by English law, will contain the usual kind of clauses one finds in such guarantees and will be supported by a legal opinion in the usual form by a Japanese law firm confirming that it is legally binding and enforceable against Fujitsu.

In addition, ICL will enter into such documentation as shall be necessary to ensure that it continues to be bound by its existing guarantees.

[The parties are to consider an increase in the £200m liability cap (in contracts and guarantees) to reflect the extension of the terms and the scopes of the contracts.]

L. Binding Documentation

The parties to work together to produce a legally binding agreement as soon as reasonably practicable. Such an agreement will be expressed to be in full and final settlement of all existing claims and counterclaims in respect of the Related Agreements and each party will acknowledge that it is not aware of any other facts or circumstances in existence at the date of the binding agreement which it is aware are likely to give rise to any such claim or counterclaim.

M. Confidentiality

Each party agrees to keep confidential and not to disclose to anyone else the existence or the terms of this document or the negotiations relating thereto (together "Confidential Information").

Notwithstanding the above, any party may disclose Confidential Information:

- (i) if and to the extent required by law;

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- (ii) if and to the extent that the other parties have given prior written consent to the disclosure;
- (iii) to its professional advisers;
- (iv) to the extent requested by H.M. Government; or
- (v) if and to the extent that the Confidential Information falls into the public domain without breach of any applicable confidentiality obligation (including this paragraph).

In the event that Confidential Information is disclosed by any party to its professional advisers, that party shall procure that its professional advisers comply with the restrictions contained in this clause, mutatis mutandis.

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SCHEDULE 1

PRE-CONDITIONS TO WHICH AGREEMENT WILL BE SUBJECT

1. [Satisfactory due diligence by POCL, BA and ICL Pathway as to the financial consequences of the agreement and of the achievability of the revised programme timetable.]
1. Satisfactory resolution of any legal or regulatory issues, including, without limitation, public procurement constraints and including any other government requirements.

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SCHEDULE 2AMENDMENTS TO CONTRACTS REGARDING ACCEPTANCE

1. Acceptance Definitions

"Core Observation Period" means the 10 week period commencing on the date falling two weeks after the commencement of the Single Benefit Live Trial Period.

[How is the Core Observation Period to be adjusted (if at all), if the Single Benefit Live Trial Period is adjusted?]

"NR2" means POCL Infrastructure, APS, EPOSS, OBCS, CMS, BES (single and multibenefit), PAS and On-line CAPS (emergency payments and stop notices) [but excludes On-Line Enquiries (OLE) and Soft EVP].

[ICL Pathway's view is that OLE is covered by CCN 124 and to be delivered as an increment to NR2 and that Soft EVP is the subject of an Agreement to Agree.]

"NR2+" means modifications and enhancements of NR2 functionality [(other than in respect of Acceptance Incidents relating to NR2)], Soft EVP, AP Smart and support of PSTN connected Post Offices.

[The parties acknowledge that there is no Acceptance of NR2+ in the same way as NR2 because the consequence of any particular facility in NR2+ not passing through Release Authorisation is that it will simply not be put into service.]

[What is meant by "contracted functionality"? Is it the same as NR2?]

"Single Benefit Live Trial Period" means, in respect of NR2, the period commencing on [●] and ending on [[●] OR the date 15 weeks after the commencement date].

[If the Single Benefit Live Trial does not start on time, does the Single Benefit Live Trial Period still run for 15 weeks?]

[Attach baseline Horizon Programme plan.]

2. Timing of Acceptance

2.1 If, at the end of the Single Benefit Live Trial Period, there has been, in respect of NR2:

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- (i) successful completion of acceptance testing;
- (ii) resolution of substantive faults raised under Paragraph 2.9, Schedule A07 of the Authorities Agreement (i.e. a default as defined under paragraph 6.1(d) of that schedule); and
- (iii) a fixed time agreed to cure other outstanding faults, *[To be clarified.]*

then NR2 shall be accepted.

2.2 No New Acceptance Incidents may be raised after the end of the Core Observation Period. "New Acceptance Incident" means any Acceptance Incident which had not occurred before the end of the Core Observation Period. Any Acceptance Incident that occurred before the end of the Core Observation Period but is not reported until after that date is not a "New Acceptance Incident".

2.3 A Joint Acceptance Board (JAB) *[define]* will be convened within the last three weeks of the single benefit Live Trial period to assess the overall outcome of Acceptance Testing, to review outstanding Acceptance Incidents and to review the outcome of disputed Acceptance Incidents sent for consideration by the Expert. The JAB will comprise [●].

2.4 The JAB will be obliged to determine whether NR2 is to be accepted not later than the date three weeks after the date on which ICL Pathway submits that all NR2 acceptance criteria have been satisfied (which date the parties acknowledge may be after the end of the Single Benefit Live Trial Period).

3. Thresholds for Acceptance Incidents

Acceptance will not occur if in respect of the outstanding Acceptance Incidents there are one or more high severity deficiencies [(also known as category (a) faults)] or there are more than 20 medium deficiencies [(also known as category (b) faults)].

4. Acceptance Incidents

The Authorities reserve the right to raise substantive faults beyond those defined in the Acceptance Specifications as described in Paragraph 2.9, Schedule A07 of the Authorities Agreement. In addition, in re-testing any corrected Acceptance Incidents, the Authorities shall have a right to raise new Acceptance Incidents which are apparently caused by the corrections.

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5. Consequence Of the NR2 Acceptance Decision

5.1 If NR2 is accepted then:

- (i) POCL and BA agree to waive their respective rights to terminate the Related Agreements as a result of non-acceptance of NR2 or any subsequent release (but without prejudice to all other grounds for termination and all other remedies for, and the consequences of, failure to achieve acceptance of any subsequent release); and
- (ii) the payment guarantees in respect of non-benefit services will commence in accordance with paragraph D of this document.

Once Release Authorisation for NR2 has been given, full national rollout of NR2 shall commence. Acceptance is not equivalent to Release Authorisation.

5.2 If, at the end of the Single Benefit Live Trial Period, NR2 is not accepted, the provisions of the Related Agreements shall apply.

The parties confirm that the Authorities shall have the right to claim liquidated damages against ICL Pathway if NR2 is not accepted at the end of the Single Benefit Live Trial Period for each of the first 13 weeks by which acceptance is later than that date. The amount of liquidated damages is to be determined in accordance with Schedule C5 of the Authorities Agreement.

5.3 If, at the end of the Single Benefit Live Trial Period, the parties do not agree as to whether NR2 should be accepted, then the dispute resolution provisions set out in paragraph 7 of this schedule will apply.

6. Appointment of the Expert

The parties have agreed to appoint an expert (the "Expert") as soon as reasonably practicable to assist in resolving disputes relating to acceptance of NR2. The Expert is to be [•].

[What are the terms of engagement of the Expert. Who bears his costs? What happens if the chosen expert is not available at the relevant time?]

7. Acceptance Disputes

[Timetable for each stage of the dispute resolution process to be agreed.]

7.1 If the Authorities and ICL Pathway do not agree on:

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- (i) the Acceptance Specifications;
- (ii) whether an event or occurrence is an Acceptance Incident;
- (iii) the assigned severity of an Acceptance Incident; or
- (iv) [a fault is a substantive fault] OR [that a substantial fault *[Is this the same as a high severity deficiency?]* has been resolved],

the parties will refer such dispute (the "Dispute") to the Expert to obtain initial guidance. [The parties do not expect the identification and notification of the Dispute, reference of the Dispute to the Expert, and obtaining his initial guidance should take longer than seven days.]

- 7.2 Once the Expert has given to the parties his initial guidance on the Dispute, the Managing Director of POCL and the [Commercial] Director of ICL Pathway shall meet and attempt to resolve the Dispute with the advice and guidance of the Expert.
- 7.3 If the Dispute is not resolved during the meeting pursuant to paragraph 7.2, then the Expert shall be required to make a decision (the "Decision") as to how the Dispute should be resolved.
- 7.4 Once the Decision has been made, the Managing Director of POCL and the [Commercial] Director of ICL Pathway shall meet to review and respond to the Decision.
 - (i) If the parties agree with the Decision, the Dispute shall be resolved in accordance with the Decision.
 - (ii) If a party disagrees with the Decision, that party may nonetheless agree to be bound by the Decision and the Dispute shall be resolved in accordance with the Decision. *[What is the difference between (i) and (ii)? Is it the right to sue later in the case of (ii)?]*
 - (iii) POCL may veto the Decision if:
 - (a) POCL disagrees with the Decision and provides to ICL Pathway written reasons for such disagreement; and
 - (b) asserts a Veto Ground (as defined in paragraph 7.7 of this Schedule).

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7.5 If POCL vetoes the Decision and the Decision was in favour of ICL Pathway then ICL Pathway shall be entitled to apply under the change control procedure for an appropriate extension of time and for compensation for additional expense.

7.6 If POCL vetoes the Decision, the Managing Director of POCL and the [Commercial] Director of ICL Pathway shall meet and attempt to resolve the Dispute but unless otherwise agreed, the veto will stand.

7.7 Each of the following shall be a Veto Ground:

(i) [●]

[Encapsulate agreed veto grounds based on D Miller letter.]

8. Release Disputes

If the Authorities disagree with ICL Pathway as to the readiness release of NR2, then ICL Pathway may require the Expert to advise on the state of readiness [of NR2]. The Expert's advice will not be binding on the Chair of the Release Authorisation Board [define].

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SCHEDULE 3AMENDMENTS TO CONTRACTS TO FACILITATE BORROWING

[This schedule is primarily based on the POCL funding paper (which has not been wholly agreed by ICL) with reference to the second ICL funding paper in respect of compensation on termination.]

1. Conditions

The changes in this schedule will not come into operation until the Pathway system has been fully accepted; National Rollout [check definition used in the acceptance schedule] has taken place successfully and financing has been successfully raised.

2. Termination by the Authority

2.1 Termination by the Authority will be as set out in the Related Agreements. However, the parties will review and seek to agree:

- (i) changes to the trigger events for termination (to add materiality); and
- (ii) what constitutes serious or persistent breaches of service levels.

[This process should, if possible, be finalised before this document is settled. ICL Pathway to revert on proposed changes.]

2.2 "Force Majeure" is to be defined by strict reference to the draft Treasury Guidelines, which define Force Majeure as:

- War, civil war, armed conflict or terrorist attack affecting the United Kingdom; or
- Nuclear, chemical or biological contamination; or
- the effect of pressure waves caused by devices travelling at supersonic speeds.

Force Majeure conditions would only apply if the above events occurred and resulted directly in ICL Pathway being unable to perform its contractual obligations. In such circumstances, ICL Pathway would mitigate any loss suffered and not claim relief from liability unless the effect of Force Majeure events prevented ICL Pathway from being materially able to comply with its

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contractual obligations and the parties could not agree within a limited period [specify] as to how to continue with the Project [define].

3. Partial Termination

3.1 The Authorities are to retain their existing rights to terminate a part, rather than the whole, of the Project. [A regime is to be adopted which is consistent with, and proportionate to, the other termination and compensation provisions.] OR [insert agreed regime]

3.2 If there is partial termination of the Project, there will be a [commensurate] step-down in the guaranteed payments after payment of any compensation payments (if any) as a consequence of such partial termination.

[Step down mechanism to be agreed.]

4. ICL Pathway's Right to Terminate

Pathway may terminate the relevant Related Agreement if:

- (i) An Authority fails to pay an amount which it is required to pay under a Related Agreement, which amount is in excess of £30,000,000 or an amount equal to the guaranteed payments due over the most recent three month period, whichever is the higher (such amount being net of any amounts owing by ICL Pathway that the Authority is entitled to set off under the terms of the Related Agreement), within 45 days of a written reminder having been received from ICL Pathway, and which amount is not the subject of any [bona fide] dispute between the Authority and ICL Pathway;
- (ii) Force Majeure occurs (and ICL Pathway has taken all steps necessary to mitigate its effect); or
- (iii) The Authority expropriates any of ICL Pathway's assets (so as to impair materially ICL Pathway's ability to perform and subject to the Authority having the right to take steps [specify?] to remedy the expropriation after a reasonable notice period).

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5. Compensation on Termination

[The following changes are based on ICL Pathway's proposal which BA and POCL are yet to accept but are included for discussion purposes.]

- 5.1 For clarification, this section addresses the circumstances in which compensation payments are made to ICL Pathway (or the lenders) from either the Authority or Fujitsu. Provisions regarding compensation payments from ICL Pathway to the Authority shall remain as stated in the Related Agreements (subject to resolution of commercial issues, including the adequacy of the current limit on ICL's or ICL Pathway's liability given the increased scope and duration of the Related Agreements).

The provisions on compensation payments set out below are subject to a specific, detailed financing plan being agreed with ICL Pathway and arranged by lenders. It is also subject to Pathway agreeing to mitigate any loss suffered.

[ICL Pathway to provide financing plan.]

The following definitions in the proposed compensation payment regime will apply:

"Lender Liability" means third party limited recourse financing to the extent that the aggregate does not exceed £[•];

"Equity" means ICL equity or loan stock and third party equity raised to the extent that the aggregate does not exceed £[•];

"Return on the Equity" means £[•];

[For refresh costs, see paragraph B of this document.]

5.2 (i) Voluntary Termination and Termination on Authority Default

[If there is voluntary termination by the Authority or termination on Authority Default, then the compensation paid to ICL Pathway should be the aggregate of Lender Liability (to the extent raised), Equity and Return on the Equity, together with breakage costs of any funding and hedging agreements of ICL Pathway relating to the Lender Liability.]

(ii) Compensation on Pathway Default

[If the Authority terminates the Related Agreements for Default by ICL Pathway, then a comparison (the "Value Test") of the costs of replacing

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the Pathway system against the costs of rectifying/repairing the Pathway system will be carried out.

If it is cheaper to repair rather than replace, then ICL Pathway shall transfer to the Authority [(or to its order)] the assets comprising the system (which for the avoidance of doubt shall not only include the physical assets but also IPR, licences and any other contracts or information required to operate the Pathway system).

If it is not cheaper to repair than replace, then the Authority shall have the option to require ICL Pathway to transfer the assets (as defined above) to the Authority.

The Authority shall pay to ICL Pathway in return for the assets an amount (the "Asset Price") which reflects the expected future cashflows of the Project less the costs of the Authority to continue with the Project under the terms of the Related Agreements. This is without prejudice to any other claims and liabilities arising as a result of the termination.

The application of the Value Test and the method of calculating the Asset Price will be determined in accordance with the Annex to this Schedule.]

(iii) Termination on Force Majeure

[Where termination is as a result of Force Majeure then the Authority shall be obliged to purchase the assets (which for the avoidance of doubt shall include not only the physical assets, but also IPR, licences and any other contracts or information required to operate the Pathway system) and the Authority shall pay to Pathway in return for the assets an amount equivalent to the market value of the assets to POCL. OR [use Value Test and Asset Price as above]]

5.3 Payment of the Asset Price to Pathway shall be made net of any set-off in respect of any claim whatsoever.

5.4 These principles shall be reflected proportionately in the regime that will apply upon partial termination.

[Regime to be agreed.]

6. Relief and Compensation Events

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If an Authority's Default precludes ICL Pathway from fulfilling an obligation under the relevant Related Agreement, ICL Pathway will be provided with additional time to perform that obligation (provided causality between the Authority's Default and ICL Pathway's failure to perform can be proven) and will be paid the higher of the guaranteed payments and transaction payments based on the actual number of transactions during the continuation of the effect of the Authority's Default.

7. Direct Agreement and Lenders' Security

POCL accepts in principle the request for a Direct Agreement (in a form satisfactory to the Authority), which would allow lenders:

- (i) to step-in and undertake ICL Pathway's obligations under the Related Agreements (provided they remain within the existing timescale for remedy);
- (ii) to appoint a substitute entity to replace ICL Pathway (provided they remain within the existing timescale for remedy and the Authority consents to such appointment (such consent not to be unreasonably withheld)); and
- (iii) to take security under the Agreement. Such security shall be limited to ICL Pathway's assignable rights and benefits under the Related Agreements, and shall not include any other assets.

8. Corrupt Gifts

8.1 Subject to any applicable statutory requirements (including, without limitation, the Prevention of Corruption Act 1889-1916), if an employee or sub-contractor provides a corrupt gift (which shall be of a material amount) without any connivance by ICL Pathway, ICL Pathway shall be allowed 30 days to [terminate the contract of the employee or sub-contractor] OR [remedy the corruption], and if it is not remedied within that time frame, the Authority may terminate the Agreement.

8.2 [In the event of corporate corruption i.e. corruption involving the board of ICL Pathway, the Authority may terminate the Agreement without a 30 day cure period.]

9. Dispute Resolution

[The provisions of the Related Agreements regarding dispute resolution shall continue to apply, save that the process in the Related Agreements shall be

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widened to include a commercial/contractual expert for
commercial/contractual disputes.]

10. Interest on Late Payments

In circumstances where the Authority makes a late payment to Pathway, or
Pathway makes a late payment to the Authority, the applicable interest rate on
the overdue amount shall be LIBOR [plus [•]%].

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ANNEX TO SCHEDULE 3PAYMENT FOR ASSETS

[ICL Pathway to revert on proposals for the Value Test and the Asset Price.

POCL's requirements, however, are as follows:

- (a) Value Test to be applied in respect of all ICL Pathway Defaults (not just performance related Defaults).*
- (b) If the Value Test fails, then the Authority has the right to purchase the assets for the higher of £1 and the Asset Price.*
- (c) No compensation shall be paid if termination occurs before full Rollout.*
- (d) The Asset Price shall be such that POCL would not be worse off as a result of termination compared with the position it would have been in had ICL Pathway complied with its obligations in full and in accordance with the agreed timetable.*
- (e) [Add more specific comments?]*

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SCHEDULE 4RESOLUTION OF OUTSTANDING DISPUTES

1. Unbundling/Transaction Metrics

The transaction metrics are to be defined in accordance with the Annex to this Schedule. In return, Pathway is to be granted a further price increase which equates to a £35 million NPV on the volumes assumed in the Corbett discussions (but, for the avoidance of doubt, has a greater value if actual volumes are greater). This price increase is to be achieved by increasing the Servicepoints for the Counter Terminal column of the Scorecard by 1.1, giving a new figure of 6.7.

[Attach copy of letter dated 21st December, 1998 to D. Murphy of Societe Generale from K. Baines of POCL?]

2. Modifications

Pathway will meet the first £37 million of the cost of modifications (inclusive of the cost of providing flat screens in non-Crown offices and inclusive of the contribution referred to below). POCL will meet the next £6 million. Pathway will meet any remaining costs.

Pathway agrees to cover the costs of any additional modifications needed to accommodate PIN pads, on the public side of the counter, for post offices in which surveys are carried out after the date agreed for installing PIN pads.

The costs of Pathway out of hours working where required are to be agreed. The reasonable costs of maintaining power supply at National Lottery node Post Offices are to be borne by Pathway.

As a contribution to modifications POCL will pay £5 million on a phased basis as modifications are carried out at a unit rate to be agreed over the total period of the modifications.

It is acknowledged by the parties that they intend to manage modifications with a view to minimising all the costs thereof.

3. Training

Pathway has agreed to provide further training in accordance with CCN 286(b) or an alternative method of providing additional training costing Pathway no more than CCN 286(b).

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4. Beat-rate Delay

If rollout is changed or delayed from the agreed Programme plan:-

- (i) to the extent that such change or delay is due to the default of either POCL or Pathway that party will compensate the other for the costs of such delay (the consequences of delay to be dealt with in accordance with change control procedures); and
- (ii) to the extent that such change or delay is not due to the default of either POCL or Pathway such losses will lie where they fall.

5. In-office Data Migration

Pathway will pay POCL up to a maximum of £5 million for in-office data migration, on the basis of an agreed specification.

[What is the process for agreeing the disputes which are listed below but are not dealt with above?]

[The outstanding disputes are listed as follows and are taken from the document entitled "Outstanding Contractual Issues as at October 1998" which contains more detailed information on such matters

1. Benefit Migration
2. Loss of Family Credit and Disability Working Allowance
3. CCN 105 (1997 Replan)
4. Extended Verification Process (EVP): CCN 243 submitted on 20/4/98
5. Outlet Modifications
6. In-office data migration
7. Steady-state Training
8. Transaction Metrics
9. CCN117: submitted 7/4/97 in response to Change Request P0016b dated 12/3/97
10. CCN251

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11. CCNs in the pipeline

The following CCNs have been submitted for more than 2 months:

- (a) CCN323 - V2.1 of CCD/CRD list
- (b) CCN90 - Call Logging
- (c) CCN297 - War Pensions Order Books Being Amended
- (d) CCN307a - Amend the Card Expiry Period at the Post Office Counter from 56 to 90 days
- (e) CCN121a - audit Schedule A03
- (f) CCN202 - Electronic Weighing Scales (to deal with the need for Weights and Measures Certification upon automation)
- (g) CCN142e - Amendments to Scorecard in Respect of BES Subsequent Transactions
- (h) CCN235a - PAS/CMS Help Desk Enquiries by BA staff pending CAPS On-line Enquiries
- (i) CCN284 - Measurement of Printer Times
- (j) CCN305 - SLA for Helpdesk "Calls not Answered"
- (k) CCN308 - PUN Information Notes (A2A R968)

12. Agreements to Agree]

[Additionally, there is a dispute involving the BES/PAS boundary.]

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ANNEX TO SCHEDULE 4TRANSACTION METRICS FOR CHARGES

It is proposed that transactions should be counted for charging purposes according to the following rules. The default is that 1 customer-facing transaction in reference data = 1 chargeable transaction. The following are the main exceptions:

Transaction items: 1 chargeable transaction per transcash item. For the avoidance of doubt, there will be no chargeable transaction associated with the fee payable on the transcash item.

Postal orders: 1 chargeable transaction per customer session, regardless of number of postal orders sold. For the avoidance of doubt, there will be no chargeable transaction associated with the fee(s) payable on the postal order(s). Where postal stamps are sold to make up the odd amount of a postal order value (e.g. the 27p of a postal order of value £35.27), these stamps will be counted as a chargeable transaction in accordance with the metrics for postal stamps (see below).

Phone cards: Sales of phone cards to be rolled up within a customer session, according to value to determine chargeable transactions. For example, if a customer buys 2 x £2.00 cards this would be 1 chargeable transaction, however if the customer buys 1 x £2.00 and 1 x £5.00 cards this would be 2 chargeable transactions.

Saving stamps: 1 chargeable transaction per client, per customer session regardless of the quantity and combination of saving stamp values sold. For example, if a customer buys 1 x £2.00 and 2 x £5.00 British Gas saving stamps and 2 x £2.00 BBC licence stamps this would result in 2 chargeable transactions.

Postage stamps: Sales of postage stamps within a customer session to be rolled up into 1 chargeable transaction regardless of quantity and combinations of stamps sold. For the avoidance of doubt, postage stamps includes definitive and special issue stamps of all values, stamp books, and postage-paid stationery. It does not include other postal products such as datapost or special delivery. For example, if a customer buys 2 x 1st class, 42p of other postage, 3 x stamp book (10 x 2nd class) and a book of 10 x 1st class stamps, this would be 1 chargeable transaction.

Because it is recognised that the volumes of postage stamp sales in the Workload Brief is subject to statistical uncertainty in deriving the average value of transactions, the charges will if necessary be adjusted retrospectively as follows:

- The actual average value of stamp sales per transaction will be calculated by dividing the total value of stamp sales recorded on Horizon by the number of customer sessions in which stamp sales were recorded.

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- The intended average value of stamp sales will be calculated as £2.51 multiplied by the average RPI for the relevant invoicing year and divided by the RPI for the year ending February 1996.
- The adjusted amount payable for postage stamp sale transactions will be calculated by multiplying the charges by the actual average value and dividing by the intended average value, any under or over payment will be included as an adjustment to the next monthly invoice.
- This adjustment will be calculated annually during the roll-out, and a final adjustment factor, to apply in all subsequent years, will be calculated at the end of the first full invoicing year following completion of roll-out.

Retail items sold over the post office counter: Charged as 1 transaction per line, i.e. 1 item of each of 2 different lines = 2 transactions, 2 of the same line = 1 transaction.

Entry of sales not transacted through Horizon: i.e. postshop, vending, lottery etc.
Charged as 1 transaction per batch entry for each product (e.g. 60 lottery ticket sales and 60 vending items = 2 transactions).

Reversals: Where transactions are subsequently reversed, the transaction itself will be chargeable as usual, but the reversal will not be chargeable, but any related fresh transaction will be chargeable.

Use of scales: Each price look-up for postage items using the scales link or by manually keyed input will incur a transaction charge for the EPOS Scales transaction in the Day 1 scorecard (scoring under Terminal, EPOS, Scales, SIS batch and no other columns) unless the counter clerk aborts the transaction without proceeding to a subsequent stamp sale transaction. These scales transactions will only be initiated by the clerk selecting them from the screen or keyboard, and will not be initiated by customers placing items on the scales without clerk intervention.

Premium Mails Services: Each item requiring separate entry will count as 1 transaction (e.g. posting 3 datapost packages which require separate recording). Where items are entered as multiples (e.g. posting 2 parcels of the same weight with recorded delivery to the same zone) these will count as a single transaction.

Scales, premium services, and postal order transactions are additional to any related sale of postage stamps, but no more than 1 postage stamp sale will be recorded per customer session regardless of the use of those stamps.

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SCHEDULE 5

REVISED PROGRAMME TIMETABLE

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SCHEDULE 6

VOLUME AND PRICING ASSUMPTIONS

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SCHEDULE 7

POCL/BA AGREEMENT

[Not to be shown to anyone other than BA or POCL. See document number
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