

In Strictest Confidence

POET(06)2nd
POET 06/01 – 06/15

Post Office Limited

(company no. 2154540)

Minutes of the meeting of the Board
held at 148 Old Street, London
on May 17th 2006

Present:

Alan Cook	Managing Director (Chair)
Ian Anderson	Human Resources Director
Simon Carter	Acting Director of Marketing & Direct Sales
Peter Corbett	Finance Director
Ric Francis	Operations Director
Graham Halliday	Banking & Financial Services Director
David Miller	Chief Operating Officer

In attendance:

Andrew Edwards	Purchasing Services, Royal Mail Group (for POET 06/07)
Ninian Wilson	Group Procurement Director, Royal Mail Group (for POET 06/07)
Neil Owen	Notes

Apologies: None

POET06/01 MINUTES OF PREVIOUS MEETINGS POET(06)1ST

- (a) The Board approved the minutes of the EC meeting of January 18th 2006.

POET06/02 STATUS REPORT

- (a) The Board noted all status report actions as completed.

POET06/03 MD's BUSINESS

- (a) POL Strategy: A number of strategy sessions had been scheduled which would feed into the RMH Strategy Event in July;
- (b) Executive Team Objectives: Interim 6 month objectives had been agreed for all members of the executive team;
- (c) Sales Goldmine: It has been agreed that Bureau targets should be for value rather than volume. A revised table for DMBs had been agreed in order to focus sales on the right

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- places;
- (d) Rapid Deployment: A Rapid Deployment review had been undertaken and agreed;
 - (e) Investment: It was reported that the following matters had been agreed at the weekly meeting of the Executive Team:
 - (i) CMA and CWU Bonus Schemes;
 - (ii) Card Account Migration (budgeted spend only)
 - (iii) Pin Change;
 - (iv) Automation of A&L Corporate Banking Transactions;
 - (v) Renegotiation of the NS&I contract;
 - (vi) A conversion/closure programme of 1.6m, together with £0.8m for unplanned maintenance;
 - (vii) £5m of additional marketing spend had been agreed (subject to no further sales expenditure being required). The cost of £3m is offset by a £2m net contribution which would result in a need to drawn down £3m from the transitional pot;
 - (viii) Allocation of the £20m transitional pot had been agreed, subject to final business case approval;
 - (ix) A risk and opportunity document had been produced for the 2006/07 plan;
 - (x) A gifting product strategy had been agreed which would involve the option to exit the flowers market within the next 4-6 months and reposition gift vouchers (the focus being on high street vouchers as a transactional product).
 - (f) Bill Payment: A bill payment strategy review had taken place, and it had been agreed to proceed with an option to invest but under a new framework. A plan would be produced;
 - (g) Organisation Design: The Organisational Design review was underway. Alan Cook would be discussing with Group the redundancy sign-off change.

POET06/04

**CRUSADER HOUSE CASH DEPOT BUSINESS CASE
POET(06)01**

- (a) Ric Francis presented the business case to the Board. The Board noted that:
- (b) the explosion at the Buncefield Fuel Storage Depot in December 2005, had resulted in significant damage to Crusader House, which the proposed investment sought to repair. This was an important strategic site for Cash Services and a key part of the future secure network strategy that was fundamental to the delivery of current business plan initiatives;
- (c) the unit accommodated 150 Post Office Cash Services employees delivering Bureau, Cash In Transit (CIT), Safenet

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and Coin processing services, and was used to store high value items for distribution across the Post Office Ltd. network;

- (d) contingency arrangements were in place at Breakspear House, but there was an increased risk to staff and cash holdings. Concurrence had been given by Cash Services that both management and employees were committed to returning to Crusader House as soon as the building had been repaired;
- (e) the investment would produce an incremental negative post tax NPV of £358k over the 7 years remaining on the lease. This resulted from the timing difference between actual costs incurred in 2006/07 and the expected receipt of the insurance claim in 2010/11. The 4.5% interest rate applied to the recovery of costs and was set against the group investment hurdle rate of 11 %. The investment resulted in a 4.5% IRR;
- (f) the proposal would impact cash flow. However, the P&L would be unaffected as costs had been included in the balance sheet as 'deferred' income until the claim was fulfilled.
- (g) Post Office Ltd. Executive Team had confirmed the requirement for this operation to continue at a meeting on 8th May. Group Investment Appraisal understood this was the least cost option available to comply with the legal, safety and security requirements for the operation to continue, and therefore had recommended the investment be approved.
- (h) After some consideration, the Executive Team agreed to the investment of £2.6m.

POET06/05

INDUSTRIAL RELATIONS STRATEGY

- (a) Ian Anderson provided a presentation on Industrial Relations strategy to the Executive Team. The following matters were discussed:
 - (i) the current status of the relationship with the union, of both Royal Mail Group and Post Office Ltd;
 - (ii) basic pay negotiations;
 - (iii) Bonus negotiations;
 - (iv) the progress being made in Cash in Transit depots.

The Executive Team noted the current status of the relationship with the Union, and agreed that:

- (i) given the new legislation that would come in effect on October 2006, the issue of seniority and holiday entitlements would be discussed at the next

Action:

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Dave Miller
Action:
Ian Anderson

Action:
Alan Cook

- Executive Team;
- (ii) Ian Anderson and Ric Francis would discuss further the situation at CIT depots;
 - (iii) Alan Cook would discuss with Adam Crozier and Tony McCarthy the possibility of writing to staff to outline the management position on basic pay and the bonus (and the timing of such a communication).
 - (iv) POL's Industrial Relations policy would continue to be carefully aligned to the Group position.

POET06/06

FRANCHISE TRIAL WITH WH SMITH POET (06)02

- (a) Dave Miller presented a paper to the Executive Team which proposed a franchise trial with WH Smith. The Board noted that:
- (b) the proposal was to transfer of 6 Directly Managed Branches (DMBs) to franchise status with WH Smith. These 6 franchises would form a 3 year pilot scheme, which, if successful, could lead to the rollout of 50 DMB conversions, with an upper limit potential of 75. The P&L benefit of a 50 branch rollout would be of the order of £10m, and this would represent a significant contribution toward the aim of 300+ long-term DMBs. The trial itself would generate an incremental post tax NPV of £ 0.9m (@11% discount rate) over 5 years and £4.1m over 10 years and was expected to improve steady state total contribution by £1.4m per annum (or £0.23m per office);
- (c) the trial activity would commence in early June with the first consultation announcement, with 6 branches live by the end of the third week in October 2006. The pilot sites would move to a five-year contract should the trial lead to roll-out (a decision on this was expected in the last quarter of 06/07) and the roll-out branches would be on the basis of 5 year franchise contracts. In order to achieve a 50-75 branch rollout, up to 100 branches would have to be ring-fenced now, because of issues such as landlord's consent; floor loadings etc;
- (d) the franchised branches would featured the open-plan design, although the cost would be a challenge. It was possible that WH Smith would help meet the costs of this fit out.
- (e) the Executive Team discussed the proposal. In the light of the economic benefits that would result, together with the consistent strategic fit in terms of headcount and DMB strategy, the Executive Team agreed to proceed to transfer 6 Directly Managed branches to franchise status with WH Smith, subject to contract finalisation and individual business cases.

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POET06/07 THE UTILITIES DIRECTIVE POET(06)03

- (a) Peter Corbett introduced Ninian Wilson and Andrew Edwards from Group Procurement to the Executive Team. A presentation was provided on the impact of the changes to Public Procurement Law (PPL) on Post Office Ltd, and how these changes would be managed. It was noted that:
- (b) currently PPL applied to 'the postal business of the Post Office' and this was interpreted to applying to the letters element of the Group business and excluding Post Office Ltd;
- (c) in 2009 a new EU utilities directive will come into force which will effectively remove the exclusion;
- (d) purchase contracts with an aggregate value above £280k would require a call for competition in the form of an OJEU advertisement, and a number of processes would need to be followed for Competition, Evaluation and Contract Award;
- (e) some areas of activity would have potential exemptions, which would include goods for resale, where there was only one possible supplier, and where the supplier was on an 'approved' list. There was also an exemption for parts of the business already operating within a fully competitive market;
- (f) analysis of POL's contracts in 2005/06 suggested that 25 would have exceeded the £280k threshold. These would need to be carefully planned to ensure the addition bureaucracy did not lead to any delay;
- (g) The Executive Team agreed that Ric Francis would lead in working with Group to help identify areas of POL that operated in fully competitive markets, and would report back as necessary.

POET06/08 EXECUTIVE REPORTS

FINANCE REPORT

- (a) Peter Corbett provided the Board with a short overview of the period 1 business results:
- (b) Profit was modestly favourable against budget (£0.7m) but cashflow was slightly adverse;
- (c) The Executive Team were reminded of their obligation to keep the finances of the Company under tight review given the nature of the interim funding agreement that had been agreed and discussed in detail at the Board sub-committee meeting earlier in the morning.

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POET06/09

SALES & SERVICE REPORT

The Executive Team noted that:

- (a) Postwatch: Milli Bangerie had taken over as Chief Executive of Postwatch. Roger Darlington, who had worked for the CWU as their head of research, had been recruited. He had set up an internet 'blog' to highlight the problems experienced in franchised offices;
- (b) Queuing: The MP for Bedford had highlighted a number of queuing issues in the area which would need to be addressed.

POET06/10

MARKETING & DIRECT SALES

The Executive noted that:

- (a) Mails: Following the last POL Board, the online postage capability of the POL website had been enlivened with "Smartstamp" (for SMEs). StampNow for consumers would go live on 4th June. A reaction was expected from the NFSP;
- (b) Telephony: There were now 300,000 live customers, and Post Office Home Phone was now confirmed as number 4 in the market, behind BT, TalkTalk/OneTel and Pipex/HomeCall. However, sales had been slow in the first month of the year and had reached only 50% of target;
- (c) Government Services: A number of meetings had been held with potential ID Card partners. Discussion with Royal Mail Letters indicate the desire to form a cross-Group team as soon as possible. The latest view on the timetable was for the Government tender documents to be available with the next 2 weeks, with submissions due within 6-8 weeks. This is likely to be resource hungry, but represented a multi-million pound opportunity for the Group;
- (d) Postal Orders: The new Postal Order was launched on 27th April with excellent media and front-line colleague feedback. Alan Cook expressed concern that the words 'Royal Mail Group' appeared on the Postal Order rather than Post Office Ltd. Simon Carter would explore whether it would be to amend this to 'Post Office Ltd' due to the potential customer confusion;

Action:
Simon Carter

POET06/11

BANKING & FINANCIAL SERVICES POET(06)30

- (a) The Board noted that:
- (b) Credit Card and Debit Card Acceptance: a business risk existed over the standards for Credit Card and Debit Card

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acceptance which had been drawn up by Mastercard/Visa. POL had joined forces with the British Retail consortium to voice its concerns;

Action:
Peter Corbett
Graham
Halliday

- (c) Horizon Data Capture: an audit of the Horizon system had revealed that data taken from cards was being stored in different parts of the Horizon system in such a way that breached Data Protection requirements. A solution was being investigated;
- (d) Alliance & Leicester: A&L were pursuing further cost reductions. Peter Corbett and Graham Halliday would meet to discuss;
- (e) RFI: 9 Responses for bottom end of Card Account. The Government would issue a tender in September. Discussions with JP Morgan concerning how to deal with EDS.

POET06/12

OPERATIONS REPORT

- (a) Horizon Next Generation: The business case had now been approval by GIA, Post Office Ltd and the Royal Mail Holdings Board;
- (a) Horizon Failure: The recent outage in the Horizon system was due to human error at Fujitsu. Fujitsu had been very apologetic;
- (b) Cashholding: The cash target had been met, but it was now becoming more difficult to produce improvements;
- (a) Safenet: There had been 3 attacks on Safenet in the last 6 weeks which had resulted in an increased risk to the business.

POET06/13

HUMAN RESOURCES REPORT POET(06)32

The Executive Team noted that:

- (a) The Group Behaviours questionnaire would be provided to the Senior Leadership Group rather than the Executive Team's direct reports.

POET06/14

RAINBOW PROGRAMME REPORT

Rob Durrant reported that:

- (a) Business Development: the modelling for Business Development of Agents had been completed. A trial would commence on 5th June 2006 and would feed into the WH

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Smith franchising proposal.

- (b) Headcount: Headcount had been reduced by 157 this year, although the staff budget was slightly over budget. Significant staff reductions would be required within 6 months for the budget to remain on track.

POET06/15

CLOSE

- (a) There being no further business, the meeting was closed.