

**In Strictest Confidence**

**POB(98)9<sup>th</sup>  
PO98/106 to 122**

**POST OFFICE BOARD**

**Minutes of the meeting held on 10 November 1998  
at 148 Old Street**

**Present**

Dr Neville Bain	Chairman
Richard Close	Managing Director Finance
Jerry Cope	Managing Director Strategy & Personnel
Dr John Lloyd	Non-Executive Member
John Roberts	Chief Executive
Rosemary Thorne	Non-Executive Member
Richard Adams	Secretary
Scott Childes	Notes

Richard Dykes, Managing Director Royal Mail  
Stuart Sweetman, Managing Director Post Office Counters Limited  
Kevin Williams, Managing Director Parcelforce Worldwide

Others attending: Robert Bishopp, Group Commercial Director for item  
PO98/113

Apologies: Mike Kinski and Miles Templeman were unable to  
attend.

**MINUTES OF  
PREVIOUS MEETING**

**PO98/106**

The Board approved the minutes of its meeting of  
8 September 1998.

**ROSEMARY THORNE  
DR JOHN LLOYD**

**PO98/107**

The Board welcomed Rosemary Thorne and John  
Lloyd who had been appointed Non-Executive Board  
Members for a three year period from 6 October 1998.

**MATTERS ARISING  
POB(98)54**

**PO98/108**

The Board noted the matters arising from the  
meeting of 8 September 1998.

**CHAIRMAN'S  
BUSINESS**

**PO98/109**

- (i) The Chairman was pleased to report that Rosemary



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Thorne had agreed to Chair the Audit Committee, with Miles Templeman and Mike Kinski as Non-Executive Members. Mike Kinski had agreed to Chair the Remuneration Committee with all other Non-Executives as Members.

- (ii) The conclusions from the Post Office Review were with Ministers and it was hoped that an announcement would be communicated before the next Board meeting. Regardless of the outcome The Post Office would continue to press for the early implementation of commercial freedoms.
- (iii) Treasury and DTI had advised their acceptance, for planning purposes at this stage, of The Post Office's proposed EFL of £207m for 1999-00, as opposed to the original baseline figure of £335m.
- (iv) The Chairman drew attention to items later on the agenda which were of major importance to The Post Office. These included the need to protect and grow international business (project 'Sapphire' being key to this, PO98/110), the Horizon programme, and improved trading performance and cash flow generation from Parcelforce.
- (v) The Chairman was concerned that across the organisation a number of issues continued to be process driven, which on occasions hampered effectiveness. Improvements were expected as a result of the Shaping for Competitive Success Programme and business organisational changes. Executive Members would seek other opportunities for improvements.

CHIEF  
EXECUTIVE'S  
REPORT  
POB(98)68

**PO98/110**

- (i) Financial Performance. With the exception of Parcelforce, the Businesses were on budget, although Royal Mail was facing pressures on productivity and mails operations costs.



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(ii) Pay Negotiations. The CWU pay award for POCL employees was implemented on 1 October with a pay bill effect of 3%; this was in line with the Board's agreed remit. The Executive Committee of the CWU had recommended acceptance of a 2.7% increase for Parcelforce employees a fraction over 3% headline increase on basic pay. DTI had agreed Royal Mail's remit for CWU employees (PO98/92) and Royal Mail would seek to conclude negotiations by the end of November.

(iii) Horizon. (a) Exhaustive discussions had been held with ICL to consider the development of new structural processes and organisational arrangements which would enable ICL to demonstrate additional commercial value in support of their revised business case. As a result of these discussions a non-binding Heads of Agreement had been prepared. This was the first step towards a closer partnership arrangement with ICL and would provide them with knowledge of potential development opportunities through Government initiatives and smart cards.

(b) ICL still faced a reduction of £250m in its business case and for the programme to continue it was therefore essential that a workable solution to the financial issues could be successfully negotiated. If the programme were aborted, ICL would almost certainly take legal action against The Post Office and DSS, although legal advice was that in turn ICL could be sued for defaulting on the terms of the contract.

(c) Indications were that Government would not step in to help ICL should the programme cease.

(d) The Secretary of State would shortly be considering three options for the Horizon programme. These were: continuation, termination and continuation following a negotiated settlement.

(e) POCL's business case remained positive and management control of the programme had improved considerably to the extent that milestones were now being achieved.

(f) Automation was essential to the future success of Counters. However, this imperative would not cause the business to compromise system quality and reliability.



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(g) The Board Thanked those people employed on the Horizon programme for the considerable effort they had put in to try and make the project a success.

**ACTION**

Stuart Sweetman

Circulate to Board Members a copy of the Heads of Agreement drawn up with ICL.

- (iv) Crown Office Conversions. (a) Ian McCartney, the Post Office Minister at the DTI, had accepted that it was sensible for POCL to operate an ongoing conversions policy, but that the network should be mixed.  
  
(b) Discussions with the CWU and CMA were continuing in an attempt to set boundaries around the level of franchises. These discussions were against the background of a CWU conference resolution that there should be more Crown offices not less. Finding a workable solution was therefore proving elusive. Ian McCartney wanted a report on the outcome of discussions by the end of November.
- (v) Quality of Service. Counters' waiting times were close to target and Parcelforce quality remained high across all streams. Royal Mail's Second class quality was high but the First class stream remained disappointingly low despite the considerable efforts of the Business. Work to improve the performance of Streamline services had resulted in improvements. It was acknowledged that more radical action was required, in the international streams.
- (vi) BBC Contract. (a) The BBC had recently announced that the Television Licensing contract had been awarded to 'Envision', a consortium of SSL, Bull and WPP. The seven year contract would run from 1 April 1999.  
  
(b) The Board acknowledged the enormous effort put into the negotiations by the SSL contract team and thanked them for all their efforts.
- (vii) (Secretary's Note: the remainder of this minute has been circulated to Members on a personal basis)



**In Strictest Confidence****FINANCIAL  
OVERVIEW  
RICHARD CLOSE****PO98/111**

- (i) Profit for September was:
  - Royal Mail      £51m
  - POCL            £9m
  - Parcelforce    £(4)m
  - SSL             £0m
- (ii) Royal Mail's September result, £35m above budget, was the result of one-off payments received from the sales of Quadrant and King Edward Building.
- (iii) Group provisional half year results, which had still to be reviewed by the Audit Committee, showed a Group profit of £283m compared with a profit of £329m in 1997-98. The result would include £78m of interest. The reduced profit was mainly attributable to increased operational costs in Royal Mail and a £25m General Election benefit in 1997-98.
- (iv) The half year result would be announced close to Christmas and public relations considerations would be carefully assessed.
- (v) Royal Mail had reduced its full year profit forecast from £496m to £478m driven by mails operations costs which in turn were driven by higher mails volumes.
- (vi) Risk outweighed opportunities in Royal Mail and the Executive Committee had asked the Business to seek opportunities to balance the two.
- (vii) To protect profit Royal Mail had initiated a number of improvement actions including improvements to underlying productivity, strengthened manpower controls, optimised management utilisation of automation equipment, an austerity programme to restrict non-staff expenditure, the re-measurement of workload to reflect increased levels of A4 size flat traffic and action to implement the Interim Delivery Agreement with the CWU.
- (viii) Parcelforce had assessed its full year outturn and produced three scenarios: -£12m, -£17m and -£22m. The Plan target was -£12m, without the pensions benefit adjustment, but based on current risks and opportunities a -£17m was the most likely result.



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- (viii) Counters' full year profit forecast had increased from £30m to £35m, the result of lower development spend. Risks and opportunities were balanced at £11m.
- (ix) POCL's financial challenge was to manage its full year outturn.
- (x) The EFL was currently forecast to outturn £18m below the target of £310m.
- (xi) Capital Expenditure spend was currently £219m against a budget of £253m with a full year forecast of £510m against a budget of £525m. Less than £100m of this money was uncommitted leaving little scope for expenditure to be allocated to other initiatives.
- (xii) It was agreed that Richard Close would report to DTI forecast outturns of £478m for Royal Mail, £(12)m for Parcelforce and £35m of POCL.

**PARCELFORCE  
WORLDWIDE  
PERFORMANCE****PO98/112**

- (i) The Parcels market was exceptionally competitive with 4,000 operators trading within extremely small margins; 5% return on sales being considered good. External competitors were suffering financial difficulties with United Carriers reporting a half year loss of £5.9m. In general the market was moving to next day products operating through information rich networks and offering an increasingly tailored service.
- (ii) In terms of quality Parcelforce compared well with its competitors although they were improving quickly. Customers viewed quality as a complete service package including access to information through track and trace.
- (iii) Parcelforce profits had not grown in its history and performance was currently £5m below budget. This shortfall was the result of a reduction in international income, which accounted for 40-50% of contribution, a productivity shortfall, an accounting variance and, significantly, unbudgeted costs on SAP.



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- (iv) Current UK income trends were encouraging but with trends in the Parcels market extremely difficult to predict, it was unclear whether this performance would continue.
- (v) Action to improve revenue would include targeted advertising and increased telesales resource, improved revenue protection and increased sales channel effectiveness.
- (vi) Action to reduce weighted unit costs had to date been successful with a reduction of 3% currently being achieved. Productivity improvements were harder to secure with a variable workload making the alignment of staff and costs difficult.
- (vii) Cost control would focus on improved utilisation of transport, better operational process controls, improved recruitment and retention of staff, central overhead cost capping and the avoidance of error enforced duplication. Considerable overhead reductions had already been achieved and this left little scope for further 'real' improvements.
- (viii) Sales functionality difficulties on the introduction of the SAP system had caused significant problems and cost £2.5m in unforeseen expenditure. The level of debt had peaked at £98m and although significant reductions in the level of outstanding debt had been achieved, debts over 90 days old were significantly higher than normally experienced. No abnormal bad debts had yet materialised. Discussions with Hewlett Packard, the systems provider, had resulted in a settlement offer of £4.2m plus VAT, although this had yet to be ratified.

noted further that

- (ix) The Board had previously considered a number of ways to improve Parcelforce's performance and the current proposal to eliminate overlaps with Royal Mail was being considered by Government within the context of The Post Office Review.
- (x) Historically October and November were Parcelforce's best months financially and would have a significant impact on achievement of the 'most likely' full year forecast.



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- (xi) Overdue payments appeared to be concentrated on medium sized businesses many of whom were unhappy about the additional work they were having to undertake to account for missing invoices.

Thanked Kevin Williams for his informative presentation.

**LIBERALISATION  
OF POSTAL  
MARKETS &  
POST OFFICE  
REGULATORY  
STRATEGY  
(POB(98)70**

**PO98/113**

- (i) The European Commission was due to make recommendations by the end of 1998 on the liberalisation of postal markets. Agreement on a draft Directive was being sought by January 2000 for implementation by January 2003.
- (ii) The Government Review of The Post Office was likely to introduce an independent regulator who would have power to introduce licensed competition. The Review was also likely to recommend some market liberalisation in advance of the EU proposals but these would probably not be as far reaching.
- (iii) Key international competitors already benefited from commercial freedoms and this had enabled organisations such as Deutsche Post AG to acquire substantial stakes in DHL and Securicor. They were also acquiring a number of smaller mail operators, although it was difficult to see what strategic purpose this had. This piecemeal acquisition of mailing companies was also being pursued by La Poste. The Dutch postal administration, TPG, had the greatest degree of commercial freedom and had a clear strategy to become the world's leading logistics and express company. The Scandinavian countries worked closely together but their operation remained modest in world terms, and to develop internationally they would need to align with another major postal administration. The key private sector operators were UPS and Fedex who were both looking to expand their European networks.



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- (iv) With competitors expanding rapidly the opportunity for the British Post Office to develop and remain a world force was, without commercial freedoms, diminishing.
- (v) The parcels market was already fully liberalised. The European Union proposals were to liberalise both inward international mail and direct mail by 2003. Liberalisation by contents, as in the case of direct mail, would be virtually impossible to police. Inward international mail could also circumvent legislation by electronic transmission of content which would then be printed abroad and physically re-imported for delivery in this country by private operators.
- (vi) The Post Office's public position was that it favoured liberalisation via the progressive reduction of the weight and price threshold of the monopoly. It was therefore proposed that the existing monopoly level of 350g, or five times the first class basic weight step letter price, be reduced to 150g, or 2 times the basic weight step price, with recognition that a further reduction to 100g could be possible subject to a satisfactory outcome from The Post Office Review.
- (vii) Existing Monopoly traffic accounted for £3.5bn income. A reduction to a 150g weight step would place £300m of this income outside of the monopoly. Any move to reduce the weight step to 50-60g would be resisted.

noted that

- (viii) Operating within the monopoly provided a psychological 'comfort zone' which hampered the introduction of new working methods. A cultural change would undoubtedly occur if this false protection were removed. It would, however, reduce income at a time when cash flows were already under pressure.
- (ix) Without commercial freedoms, The Post Office could not support market deregulation.
- (x) It was important to be influencing future policy and to this end taking a proactive stance on liberalisation was supported.
- (xi) A reduction of the monopoly would be a key driver to reduce costs, particularly staff costs which accounted for 75% of Royal Mail's expenditure.



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- (xii) Understanding competitors' strategic ambitions, and how these impacted on The Post Office's own ambitions, was an important consideration.
- (xiii) Support for a reduction in the monopoly would have to be carefully communicated, with the reasons why this position was being adopted clearly set out. Communicating with the union who were currently seeking strong action to be taken against TNT for breaching the monopoly, would need proper consideration.
- (xiv) Agreed the proposed approach to liberalisation as set out in (vi) above and that alternative regulatory scenarios should be developed.
- (xv) Agreed that communication of the proposals should be carefully considered.

Action  
Jerry Cope

Address how communication of the key issues, to employees and the unions should be approached particularly explaining why they had been adopted.

**MaPEC - (1)**  
**Parcelforce**  
**Internal Logistics**  
**(POB(98)71)**

**PO98/114**

- (i) The proposal would provide a co-ordinated approach to the provision of general supplies across the organisation. Additionally, it developed Parcelforce's commercial strategy by enhancing its logistics service.
- (ii) Under the proposal a one site distribution centre at Swindon would be developed which would offer upper quartile performance when benchmarked against external competitors. All other Post Office stores and warehousing operations would close.
- (iii) Annual savings of £3.8m would be realised with one-off benefits of £17.5m.
- (iv) Endorsed MaPEC's approval for full implementation costs of £5.5m capital, £12.3m revenue, including a special DFE provision of £1.0m for EVR and relocation costs, and in principle authority for systems upgrades/replacement costs of £0.6m capital and £1.8m revenue.



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MaPEC (2) -  
Trusted Third  
Party  
(POB(98)72)

PO98/115

- (i) Trusted Third Party (TTP) provided electronic certification of identity, digital signatures and security during the transmission of messages and transactions over the Internet and intranets using encryption software. It provided The Post Office with key capabilities for the developing e-commerce market and an infrastructure for other initiatives such as Government Gateway. It built upon the considerable brand strengths that The Post Office enjoyed.
- (ii) The Executive Committee had reviewed and endorsed the proposal which positioned The Post Office as a multi-faceted supplier of choice.
- (iii) Considerable effort had gone into identifying the most suitable form of technology and the Executive were happy that suitable systems technology was now in place.

noted that

- (iv) The benefit of external investment in the project had to be weighed against the potential disbenefits that could result, as had been seen with Horizon. Before proceeding the Business would therefore need to be sure that an external investment partner would add real value.
- (v) The wider organisational benefits that TTP would bring e.g. smartcards, lottery, Government Gateway etc, could not be underestimated.
- (vi) The full service would be launched in January 1999 under the Royal Mail brand and that TTP had the potential to generate income of around £120m over five years.
- (vii) Endorsed MaPEC's approval of additional funding of £8.2m required for completion of the project to full commercial launch



**In Strictest Confidence**Action

Richard Dykes

Review the value of proceeding with TTP alone, as opposed to seeking third party investment. Report conclusions to the Board.

MaPEC (3) -  
West Yorkshire  
RDC (POB(98)73)

**PO98/116**

- (i) The existing Streamline Regional Distribution Centre was space deficient and unable to accommodate volume growth which had seen 14-15% year on year increases.
- (ii) The current site had opened in 1994 and it was disappointing that further expenditure was necessary so soon but no other satisfactory alternative existed.

Endorsed MaPEC's approval of the relocation of West Yorkshire RDC operations to a new site at Tuscany Park, Normanton. This was at a maximum outturn cost of £10m to fit out, together with an annual rental of £0.99m, giving a total authority sum of £22.9m. Further endorsed disposal of the existing estate with capital receipts of £1.7m.

AUDIT  
COMMITTEE  
REPORT  
(POB(98)74x

**PO98/117**

The Board noted the report.

CUSTOMS &  
EXCISE  
CHANGES TO  
VAT GROUPING  
REGULATIONS  
(POB(98)75x

**PO98/118**

The Board noted the report



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**MaPEC Bi-  
ANNUAL  
REPORT  
(POB(98)76x**

**PO98/119**

The Board noted the report but questioned the value that it currently brought to the Board. A more informative and beneficial report would be one that addressed post implementation issues and in particular success/failure criteria.

Action  
Richard Close

Dispense with the Bi-annual report but in its place introduce a bi-annual Post Implementation Review paper which detailed the success/failure of investment cases.

**PROJECT  
APPROVED BY  
MaPEC  
REQUIRING  
ENDORSEMENT  
BY THE BOARD -  
Norwich  
Accommodation  
Strategy  
(POB(98)77x)**

**PO98/120**

The Board noted the report

Endorsed MaPEC's approval for further expenditure of £4.11m at outturn prices to provide a new Cashco and POCL accommodation and Mail Centre rationalisation, with a DFE of £0.14m and total project expenditure of £11.15m.

**PROJECT  
AUTHORITIES**

**PO98/121**

The Board noted that the current format of MaPEC Board papers did not always clearly and concisely set out the key issues. This was a particular issue for new Board Members.

Action  
Richard Close

Consider how best to present MaPEC reports to the Board which would ensure that the key issues were easily and readily identifiable.

**DATE OF NEXT  
MEETING**

**PO98/122**

8 December 1998, provisionally commencing at 9am.