COMPANY SECRET

FUJITSU

FUJITSU SERVICES HOLDINGS PLC
FUJITSU SERVICES LIMITED
FUJITSU SERVICES (INVESTMENTS) LIMITED
(the "Companies")

Minutes of a Meeting of the Fujitsu Services Management Committee of the Boards of Directors of the Companies

Held at 1.30 pm on Thursday 18 August 2005
at

Irrelevant

Present:	Mr. R. Christou	(Chairman)
	Mr. T. Adachi	
	Mr. D. Courtley	
	Mr. H. Madarame	
	Mr. H. Hirata	
	Mr. B. Harris	
	Mr. A. Nagai	
	Mr. T. Moriya	
	Mr. K. Nozoe	
In attendance:	Mr Y. Nagano	
	GRO	(Secretary)
	Mr. H. Kubo	
	Mr. T. Nagayama	
	Mr. S. Yamasaki	
Apologies	Mr T. Yurino	

05/20 Introduction and Minutes of Meeting held on 18 May 2005

The Chairman welcomed those present at the Meeting. He explained that Mr Nozoe would be resigning from the FSMC and that Mr Nagano, who was present today, would be joining it. He thanked Mr Nozoe for his support and welcomed Mr Nagano.

Mr Nozoe said he was grateful for the opportunity of being a member of the FSMC for the past fifteen months. He was glad to have been involved and to have had the opportunity to review FS transactions both in the public and private sectors. He was not leaving Fujitsu and hoped for a deeper and broader relationship with FS in his new marketing role. The Chairman said he hoped Mr Nozoe would keep in touch.

Mr Nagano expressed pleasure at joining the FSMC and working with Mr Hirata. He referred to the visit he had made to FS in April 2005 as Marketing Director of Fujitsu Limited ("FJ") when he had spoken of the much closer marketing relationship he hoped to have with FS. He would be working with Mr Hirata in support of the Service Product Business

Group and would be making infrastructure and outsourcing activities his major activity. As a member of the FSMC, he hoped to make his own personal contribution to the advancement of FS and looked forward to learning a good deal from FS and its capabilities.

The Chairman asked if there were any comments on the draft minutes of the 18 May 2005 Meeting. The Meeting had no points to raise and approved the minutes. It was agreed that they should be signed on behalf of the Meeting by the Chairman.

05/21 Chief Executive Officer's Report FSMC/05/22

The Chairman invited the Chief Executive Officer to make his report.

Mr Courtley presented this paper, adding a few comments to what he said there.

Trends – He had been pleased with the positive reaction of analysts to the Group's results. He felt they understood the Group's strategy.

Business Continuity – He repeated his thanks for messages of goodwill from around the Fujitsu Group following the July attacks on London.

Performance Q1 2005/6 – As Mr Harris would explain, for the present FS would continue to report under UK GAAP, despite the intention to switch to IFRS. Although some of the £46.5m increase in revenue was due to the integration of FESA, some was organic growth.

Budget – The Q3 budget was unchanged for the 9 months to December for the full year.

Service Delivery – He was pleased to report that there were no red alerts at present and few amber alerts and noted the action taken to prevent recurrence of alerts caused by supplier failings. Success in the SLA achievement was still exceeding 93%.

Mid-Term Plan – He thought FS must continue to build its consultancy business. FS now had an evolving model joining up its consultancy and outsourcing activities, which was proving successful in the market place. The Mid-term Plan would speak about this.

The Chairman asked if there were any questions. There were none.

05/22 CFO's Report FSMC/05/23

The Chairman asked Mr Harris to present his report.

He explained that ratification by the FSMC of the adoption of International Financial Reporting Standards (IFRS) by FS was on the agenda for the meeting today. The Q3 budget had been prepared under UK GAAP and under IFRS. The figures for previous budgets and for the corresponding periods of 2004/05 had been restated to IFRS. In order to retain the recognition with previously reported figures he would explain the Q3 budget under UK GAAP and identify the main adjustments to IFRS. The main pack included the Summary P&L and Balance Sheet under IFRS as well as the usual schedules and analyses of their movements from UK GAAP to IFRS for all periods. There was also for reference a full pack of the Q3 budget under IFRS.

The schedules showed the Q1 results in the block on the left of the pages. The Q3 budget for the periods of Q2, Q3 and the full year were in the blocks moving across the pages to the right.

Q1 results

Mr Harris explained the Q1 results by reference to the Summary P&L on *Page 1* and to the Balance Sheet on *Page 14*.

Page 1 was the **Summary P&L** under UK GAAP. Q1 **revenues** of £484m were £12m below the Q2 budget of £496m. Most of the shortfall related to the continued delay in signing the Walsall contract in Public Sector, which was down by £8m. EMEA was £4m lower from the delay in securing the Tiscali order in Holland. The **margin** was at the Q2 budget level of 19.3%. **Opex** of £82.4m was £5m lower than the Q2 budget of £87.7m with all businesses contributing to the savings. **Rationalisation** costs of £1.1m were £1.4m lower from deferrals in Core, EMEA and Nordic. In Core, FS continued successfully to redeploy people and the Committee would remember that the budget included an allowance for rationalisation in Nordic, and in Spain (not yet applied). These costs would be incurred later in the year. **Operating profit from associates** of £3m was £0.7m more than the Q2 budget from improved profitability in Camelot, mainly from its European activities. This improvement would continue. **Operating profit** was, therefore, £12.8m, which was £5m more than the Q2 budget. The improved cash position at June had resulted in **interest income** of £1.1m being generated in the quarter. **PBT** of £14m was £6m more than the Q2 budget of £7.8m. **Orders received** of £646m were lower than the Q2 budget of £670m. The shortfalls were O2 and Telewest in Commercial amounting to £25m, the loss of Harrow at £24m in Public Sector, slippages in EMEA on the FSC helpdesk for £30m, Tiscali for £11m and from Nomura for £10m in EMEA. The main orders secured were LloydsTSB for £170m, the PwC datacentre for £65m and the CHOTS one year extension for £96m.The O2 order was signed in July. Compared with 2004/05, **revenues** were £47m more than the £435m achieved last year. Aspire contributed £32m and Spain £24m. The **margin** was almost 1 percentage point more than 18.6% last year, which was accounted for by the reduction of 1 point in 2004/05 for the effect of the Sirius benchmarking effect on prior years. **Opex** was £4m more than last year from the inclusion of FESA. **Operating profit** and **PBT** were both over £7m more than last year.

Page 14 was the **Balance Sheet**. The cash balance at June was £29m. It was £14m more than the Q2 budget, due to lower capital expenditure on the Aspire and NHS contracts. There were movements in the various lines of working capital, but the total of £136m was consistent with the Q2 budget.

Q3 Budget

Page 1 was the **Summary P&L** under UK GAAP.

The next block to the right of the Q1 results was the Q3 budget for Q2. **Revenues** of £503m were £25m less than the Q2 budget. The shortfall related equally to delays on Walsall, the slippage of VME product for DWP in Central Government and delays in EMEA. The reduction in the

FUJ00003674

margin of 1.5 points to 19% was mainly accounted for by the VME delay to DWP. Closing contracts for which FS had been selected was a major issue which Mr Courtley and Mr Harris were currently addressing, as revenue slippage was the inevitable consequence of delay. **Opex** of £82m was £6m less than the Q2 budget of £88m, primarily from continued deferrals of expenditure in Group HQ. Currently, restraints on HQ spending to secure the profit position were being held to secure the profit position. **Operating profit** of £13m was £7m lower than the Q2 budget. This reduction could be related to the delay to Q4 of the VME sale to DWP. It was compensated at the PBT level by the gain of £6.7m on the disposal of the shareholding in Infocare, which has been concluded and should be in the August results. In the Q2 budget, because of the uncertainty of the timing at that stage, it had been included in Q4. **PBT** of £18.4m was, therefore, unchanged from the Q2 budget. **Orders received** of £539m were £531m below the Q2 budget because of the continuing delay on closing the Walsall order.

The next block was Q3. **Revenues** in the Q3 budget of £594.5m were unchanged from the Q2 budget. The margin improvements that were included in the Q2 budget would materialise later than previously expected. **Gross margin** was, therefore, £3m lower at £116.9m. **Opex** deferred from the first half in Group HQ would start to be spent in the second half. It was £90.6m compared with £87.9m in the Q2 budget. **Operating profit** of £26.1m was £5.8m lower than the Q2 budget of £32m. Although **PBT** was £6.2m lower at £23.8m, cumulatively for the first three quarters, it was unchanged from the Q2 budget at £56.2m.

The full year was to the right of the page. **Revenues** of £2280.5m and **PBT** of £102.2m were unchanged from the Q2 budget. A minor reduction in the margin was compensated by improved profitability in the Group's Camelot **associate**.

The Q2 budget for **Orders received** of £3,211m and **headcount** of 19,979 were also retained in the Q3 budget. Compared with 2004/05, revenues were £294m more than £1,986m last year, an increase of almost 15%. The increase was accounted by the integration of FESA of £132m, LloydsTSB at £58m, NHS £60m more, Aspire £29m more and Walsall at £30m. Excluding FESA, the increase was 8%. The **margin** was slightly lower at 20.4%.

Opex was £29m more due to FESA. **Rationalisation** of £12m included an allowance of £7m for Nordic and FESA. **Interest** costs were offset by the higher **gain on disposals**. **PBT** of £102m was £17m more than in 2004/05.

Page 2 was the **Major Movements** in Q3 budget revenues and PBT from the Q3 budget for Q2, Q3 and the full year. The effects of the delays on the Walsall contract, the VME for DWP and in EMEA were shown on the first three movement lines. Expenditure on the Triole project was slower without detrimental effect on its progress. The next line showed that improvements in margins would materialise later than previously expected. On the next line, Opex deferred from the first half being spent from later in the year.

Page 3 was the **Analysis of the Adjustments in revenues and**

FUJ00003674

operating profit from UK GAAP to IFRS. It showed the changes relating to revenue recognition for the long-term contracts applying the percentage completion method and to pension accounting. Applying IFRS, it showed that **revenue** would increase this year by £116.3m to £2,397m under IFRS (and under the IFRS standard all costs incurred had to be charged to P&L and the appropriate level of revenue taken against them irrespective of any delivery or acceptance by the customer) and **PBT** would be £33.8m more at £136m. £8.8m related to the margin on the additional revenue. £25m related to the pension cost, where the pension deficit being written off to reserves meant that only the normal charge was charged to P&L, and the amortization deficit was not required. This gave FS a £25m increase in its profit to £136m. The analysis showed that the change in accounting mainly affects the PFI-type contracts, with revenue on contracts with a development stage being booked earlier, as the cost was incurred.

Page 4 was the **Summary P&L** under IFRS. Mr Harris noted one correction here for a mis-posting: the gain in the margin on the additional revenue had been posted to Opex when it should have been in the Margin line. The PBT numbers were, however, correct. Each period had been adjusted, including the previous budgets and last year.

Page 5 was the **Revenues by business unit**. In Q2, all businesses are below the Q2 budget with the exception of **Commercial**. At £125.7m, it is £7m higher from service revenues from Centrica brought forward from Q3. The slippage of the VME sale to DWP reduced **Central Government** to £187m in Q2 from £195m in the Q2 budget. **Public Sector** is £11m lower at £32m, reflecting mainly the delay on Walsall. The reduction in **EMEA** to £93m was due to the delays on the Tiscali and Aer Lingus contracts (the latter had been won, but Aer Lingus needed to negotiate the conditions with the unions). In Q3, additional Defence revenues in **Central Government** offset reductions in **Commercial** and in the two **European** regions. The full year was unchanged from the Q2 budget.

Page 6 was the **Margin by business unit**, which was broadly in accordance with the movements in revenues.

Page 7 was **Opex by business unit.** At £82m in Q2, it was £6m less than the Q2 budget. Most of the savings were HR, Marketing, CIS and Properties in **Group HQ**, which was £3.3m lower at £9.2m. **EMEA** was £1.5m below Q2 budget at £18.5m and **Nordic** was £1.2m less at £8.3m. Spending in the second half by **Group HQ** was, consequently, higher than in the Q2 budget. In Q3, it was £2.6m more at £13.7m, which accounted for all of the increase in the total from £87.9m in the Q2 budget to £90.6m. Opex in the full year was unchanged at £365.6m.

Page 8 was **Rationalisation** costs, which were £0.5m more than the Q2 budget in the full year, as a result of a reassessment of the sales force in **Commercial**. *Page 9* was **Operating Profit**, *Page 10* was **Orders received**, *Page 11* was the **Orders backlog** and *Page 12* was the **Headcount**, all by business unit. The movements from the Q2 budget were explained by the previous schedules.

Page 13 was the **Headcount bridge**. The main movements occurred in

Q1. The increases relating to FESA (where 1,539 people joined) and the LloydsTSB contract (where 533 people joined) were highlighted. In Q3, the additional 320 people were for new business relate to the FSC helpdesk, Aer Lingus and Walsall contracts.

Page 14 was the same presentation of the **Balance Sheet** under UK GAAP as for the Q2 budget at the last FSMC. Net borrowings would be higher throughout the year than in the Q2 budget. They would be £83m in September, compared with £60m in the Q2 budget. Borrowings would increase to £100m in December and would be £65m in March, both £35m more than in the Q2 budget. The increase was mainly due to the reinstatement of the capital expenditure programme on Aspire, in particular the e-services portal refresh for internet tax returns, the Stride project for the NT replacement by Windows XP, and the data replication project. (The Meeting would recollect Mr Harris's previous explanation that, up to now, with the integration of the Inland Revenue and HMCE by the UK Government, the capital expenditure on these had been held until they had worked out the structure. That exercise was now more advanced, and they had therefore reinstated the programme). The effect appeared in **Fixed Assets** of £323m. Net borrowings of £65m at March 2006 represented a cash outflow of £135m during the year. £27m related to the acquisition of FESA, Aspire would absorb £40m, DII £20m and NHS £100m. HMCE would generate £57m. Those contracts accounted for the main movements on FS's cash position.

The main effect on the Balance Sheet from the implementation of IFRS was the accounting for the Pension Fund deficit, which was written off against Reserves. The **Adjustments to Share Capital and Reserves** at March 2005 and March 2006 were shown on *Page 15*. It demonstrated that, from a healthy position of in excess of £400m of shareholders' funds under the previous UK GAAP FS Would at March 2006 have shareholders' funds under IFRS of £119m. Moving down the schedule, the first item was the writing off as at 1 April 2006 of the IAS 19 Pension Fund deficit of £524m with the related deferred tax effect; the previous accounting prepayment was no longer relevant and was written off to reserves, too - £52m, with the deferred tax upon it. There was, however, an improvement to FS's shareholders funds through the lower charge to the P&L for pension costs and at March 2006 FS would have two years' worth - £51m, again with a related tax effect - The annual charge to the P&L for Pension costs ceased to include the amortisation of the deficit, having been written off to Reserves. It reduced by £26m in 2004/05 and was estimated to reduce by £25m thereafter. This benefit was included in the PBT under IFRS on *Page 4*. The other adjustments related primarily to the effect on profits of revenue recognition and leases. Share capital and reserves at March 2006 reduced from £485m under previous UK GAAP to £119m under IFRS. The figure was similar to current UK GAAP with the introduction of FRS 17.

Page 16 was the **Balance Sheet under IFRS**. Each period had been adjusted, including the previous budgets and last year.

Pages 17 to 19 were the **Inventories, Debtors and Payables** by business unit, respectively. They showed that working capital in Central Government at March 2006 would be lower than the Q2 budget from payables for year end capital expenditure

Page 20 was the **Cash Flow**. The free cash outflow in the year of £129m would be £36m more than the Q2 budget from the additional capital expenditure, mainly on Aspire, offset by lower working capital in Central Government, as previously explained.

Page 21 is the **Capital Expenditure and Depreciation** schedule by quarter. The increase in capital expenditure from £188m to £249m is contract related. Much of it will be incurred in Q2, being carried over from Q1, and in Q4.

The next packs were the Attachments and the Q3 budget under IFRS for reference.

The Chairman asked if there were any questions for Mr Harris.

Mr Adachi referred to the Summary P&L on page 1 and noted the progressive increases in Net Opex – Q2: (£82m); Q3: (£90m); Q4: perhaps (£110m). If control of expenditure continued as in Q1 and Q2, would it be possible to improve Net Opex by £20m, to make it £90m rather than £110m in Q4? Mr Harris said that, numerically, Mr Adachi was correct, but in Q4 FS accrued for most of the incentive and bonus payments (assuming that FS made its numbers). The other item that occurred towards the end of the year was an e-procurement project called Lightfoot which would incur some £4m of costs on the development stage, which was in the forecast for the second half of the year. So Mr Adachi was right that, if the constraints continued, FS would improve on Opex, but he thought the improvement here would not be as much as £20m. He nevertheless admitted that there was an opportunity.

Mr Adachi also referred to the Balance Sheet on *page 14*. At the end of September, FS had borrowings of £83m. Had those borrowings already been incurred at the present date? What was the current number? And as regards the figure of £65m at the end of March, how much could FS improve that number if it tried really hard? Mr Harris replied that at the end of July FS had had £25m of borrowings. So the £29m cash at the end of June was now £25m of borrowings. FS would try very hard to improve that position and have borrowed less than £65m at year end. To that end, FS would try hard to collect cash. The Government tended at the year end to be helpful – advanced invoicing showed £150m which had been received from the MoD, and by the end of the year it was forecast to fall back to a normal level of £114m. In previous years, FS had gained by £20-30m, though he could not guarantee that this would continue. He was also looking at other things – for example, if the NHS progressed well, it might be possible to advance the advance payment from the NHS, but that was merely a hope. To sum up, he would try to improve the cash position and he hoped the MoD would continue to be helpful with advanced payments, but he could not predict how far the £65m would reduce – there were too many unknowns. But if revenues increased, it would have an effect on FS's collections. Mr Courtley added that the forecasts this time were not as good as he would have liked. He believed FS could improve but, as a precaution, some spending had been restrained to ensure the profit target was achieved. He was also seeking measures to improve the business. An example was Project Lightfoot – if the improvements were not attained, that project could be stopped before the money was spent. On balance sheet, he hoped for a better cashflow solution through the NHS which would reflect in the balance sheet. He also stressed that FS could not rely on advanced payments from the Government, but in fact there often were such payments around the year end.

Mr Hirata asked about the impact of Walsall on revenues and the current position. Mr Courtley replied that large projects were attractive, but there was a substantial impact when delays occurred. Those delays were partly due to the need to complete contract schedules, and partly to a mistake by Walsall in calculating its budgets. FS was addressing this by taking away scope and assuming a little more responsibility than previously planned through sub-contracts. It was important not to increase risk unacceptably and it was taking time to make the assessment. If all went well, he expected to sign the contract in October.

The Chairman summed up by saying that questions were raised by the Q3 Budget. Corrective measures were being taken and they were believed to counter the risks. There was, nevertheless, the possibility of upside if the risks did not materialise, though how much was a matter of conjecture. The difficulty of closing deals like Walsall was not to be under-estimated.

05/23 Implementation of IFRS — Oral report

Mr Harris said that he had not produced a Paper on this item, since he felt that a paper on such a technical subject would not be helpful in this particular Meeting. The purpose of this item was to seek the Committee's approval, on behalf of the Board of FSH, of the proposal to adopt IFRS. In European countries, quoted companies were now having to adopt IFRS and FJ had signalled its intention to do the same, perhaps next year. This year, FJ intended to go part of the way by implementing the percentage completion basis. In the UK, a company could not adopt an accounting standard in part – it was a case of all or nothing. IFRS was beneficial to FS for the pension fund accounting aspect and FS wished to comply with the corporate policy on recognising revenue. It accordingly wished to implement IFRS – hence the request for Board approval.

The Chairman asked for questions. He commented that, on the surface, it looked as though it improved the P&L and damaged the balance sheet but, whatever it did, it made no change to the cash or debt position – the underlying position was exactly the same and it was simply a different way of presenting the results.

It was RESOLVED by all those present to approve the implementation of IFRS, as proposed. Mr Harris was directed to continue his collaboration with Mr Moriya.

Mr Harris confirmed that he and Mr Moriya and their respective teams were working closely and well together on this difficult task.

05/24 Major Bids Report — FSMC/05/24

Mr Courtley presented this paper.

Item 1, Walsall – He ad already referred to this. This bid was not yet closed. He hoped it would sign as soon as possible, but the remaining issues were not easy. It was notorious that contracts with local government customers were difficult to bring to completion.

Item 2, Northern Ireland Civil Service – This was worth about £250m over fifteen years and was in its final stages of down select, with Accenture as the competing bidder. FS was bidding with PwC and Capita. David hoped for a successful outcome. It was a BPO deal and he thought it offered FS the opportunity to learn a lot through the partnerships so that, in future, it could take more responsibility itself directly and earn more margin from such transactions. The FJ EMC had recently approved FS's request for a parent company guarantee in respect of this project and he was grateful.

Item 3, IRRELEVANT – This involved desktop managed services in the telecoms sector. Part of it would involve consideration of an operation in Poland and as part of the bid FS was looking at whether it would be a good idea to consider a Polish operation on a modest scale. David thought that FS's bid was competitive with EDS, the other main contender.

Item 4, NOMS – This was another competitive bid, with Steria as the other bidder. Again, Mr Courtley was grateful for the recently approved parent company guarantee. It was a good deal in the centre of FS's standard offerings and he believed that FS was well positioned. The customer was now evaluating the bids and FS would have to wait and see the outcome.

Item 5, Post Office – This involved moving to the next generation of Horizon. At present it was difficult making a business case with the Post Office, which did not have much spare money. The negotiations were accordingly challenging, but were continuing.

Item 6, BAE Systems – It was expected that this bid would take off in November when the customer launched an RFP. This would be a big project, worth up to £2bn.

Item 7, DCA – This was the opportunity to bid for a single infrastructure contract to replace services provided by FS (Libra) and others. FS had had managed to transform the customer's view of FS, achieving high level of customer satisfaction on its existing services – over 9. This was accordingly a good prospect, despite the presence of three other competitors, including EDS, and he thought FS might be seen as a favourite to win it. FS was also conscious of the need to avoid complacency.

Item 8, United Utilities – This was a managed services opportunity for a big utilities company.

Item 9, IRRELEVANT – The customer was at last looking for a POS update and he was pleased to say that the customer was looking to buy a managed service rather than just technology. This would be competitive but, as an incumbent supplier, FS was well-positioned.

Mr Courtley then turned to new bids.

Item 10, HMRC – This involved the merger of HMCE and the Inland Revenue. As a result FS had the opportunity to increase the value of its order book through the extension of the contract length as a result of that transition. That should be a positive development for FS. It would take some time to negotiate.

Item 11, NHS – The existing PACS service was going well. FS had shown itself to be the best performing LSP and it was being given opportunities to bid in other areas – East Midlands and North-east of the UK.

Item 12, Ditech – This related to an Italian company which wished to divest itself of its internal IT services with a view to having a contract instead. FS was looking to take over those services for little or no consideration. It was, Mr Courtley thought, a good way of improving its business in Italy.

Looking at bids reported last time, the following was worthy of mention -

Item 13, PwC – Mr Courtley was pleased to report that this contract, for datacentre services over four years and worth £62m, had been signed.

Under lost and withdrawn bids -

Item 14, HMCE – This had concerned the Automated Lorry Road User Charging System. The Government had re-evaluated its strategy in this area and had withdrawn this opportunity. As a result, FS would probably be able to recover some of the money it had spent on this project.

Item 15, Inland Revenue – FS had decided not to bid for this big hardware supply project because it did not presently have the right capability or positioning.

Mr Courtley asked if there were any questions.

Mr Hirata commented that there were good deals in the pipeline, but was wondering whether there would be sufficient human resources to deal with them. Mr Courtley replied that substantial resources were needed to bid these deals. It was important to qualify strongly so that resources did not become too thinly stretched. As regards delivery, the same applied. With outsourcing deals, there was the benefit of staff being acquired and some of them (for example, on the Aspire project) were very good. That said, there were often too many contractors (as on Lloyds TSB). Another challenge was to build up the strength of the account management teams – FS could not run the risk of having unqualified people in management positions. He felt that, so far, this was being managed reasonably well. Mr Hirata wondered whether there were any resourcing issues specifically referable to the NHS prospects in other regions. Mr Courtley explained that the PACS deals mostly involved equipment, so did not impose too heavy a headcount burden. The PACS team was only ten people, but the quality of those people had been instrumental in FS's success. The challenge was to keep the quality high.

Referring to his perception of a shift in focus of FS business from the Government side towards the private sector, Mr Madarame asked what skills and resources FS thought it was currently lacking. Mr Courtley replied that there were still commercial deals coming into the pipeline, as well as Government deals, so there was a balance. The main difference between the two sectors was that sometimes the commercial sector wanted to move very quickly. The question was whether FS could adapt to that style. Opportunities like Orange required this. On the resources side, he was able to put the right people before the customer in order to win. There was some stretch, but he felt that he resources were being managed well enough. It was helpful that it had been possible to bring some good people in to supplement existing resources and, so far, capable senior people had not been lost to competitors. The skills most in demand were senior technical architects and programme managers and this was where the greatest difficulty was experienced when recruiting and where it was most important to focus FS's internal training programmes.

Mr Nagano asked about BPO prospects, such as the Northern Ireland e-HR deal. BPO involved human links and a partnering model. He wondered whether FS itself could obtain the skills it needed for such work. And what was the gross margin for BPO, and the criterion for taking BPO business? These were topical questions in Japan, too. Mr Courtley replied that FS should not enter the highly commoditised part of the BPO market. In that part of the BPO market, the typical gross margin there of 5% was far too low for FS. Instead, FS needed to focus on areas very close to IT, which were not commoditised. If it did so, he felt it could aim to achieve similar margins as those which FS achieved elsewhere in its business. It might be that slightly lower margins could be accepted, but he would look hard at a proposal where the margin was less than 20% gross; he would look very hard where it was less than 15%. In the early stages of FS's experience of partnering, of course, it was important to understand that FS would be in a learning curve and could not simply put margin on top of margin carelessly and expect to win. A learning curve was unavoidable, as FS had found with Walsall. When FS offered these services itself, it had to see them as added value services, not commoditised services, and price them accordingly. He added that BPO was not an area FS could avoid: it was an opportunity and, if FS did not grasp it, it would be naive to assume that the world was going to buy IT outsourcing on its own to suit FS. FS must face up to this gradual change in the market and adapt.

Mr Nagano added that, when doing BPO work, he found that upstream business process needed to be revised and improved. The role of business consultancy was important in this context. Was he right to assume that Mr Courtley intended to ensure there was sufficient internal resource for this activity? Mr Courtley agreed that, to succeed of selling BPO, FS needed consulting capability to be credible and to be able to do the required process redesign. So a particular business consulting group had been established in Core, headed by Robert Devlen. He hoped this would enhance FS's ability to sell and deliver with increasing credibility. There had recently been a collaborative discussion with FJ on the consultancy aspect and one of the senior FJ consultants had presented here on this subject. Some details of the FS model had recently been shared with FJ. Mr Courtley would be happy to go into more detail on this at the next FSMC.

The Chairman commented that the subject would form part of the Mid-term Plan which would be under discussion at the next FSMC anyway, so it would be addressed then. It was agreed that it would form a separate component of that Plan. **DC**

05/25 Major Accounts Report FSMC/05/25

Mr Courtley began by saying that he had not included Lloyds TSB in this present report but would do so at future Meetings of the FSMC in view of the size of the account. **DC**

NHS – Mr Courtley reminded the Meeting that FS had failed to work successfully with BT and IDX and had, with the customer's agreement, terminated their agreements. There had been risks in taking that course, but he hoped that would be accomplished safely. Looking forward, the plan now was to use Cerner as the sub-contractor instead. Having looked carefully at Cerner, he strongly believed that this was much more likely to succeed. Cerner had better plans than IDX and managing them direct, rather than via BT, gave FS more control. FS had insisted on placing a large team on the site working with them so there would be a joint effort. This would be a much healthier plan than the position up until now. The customer had been pragmatic and had agreed somewhat easier terms for delivery – they wanted FS to succeed. Indeed, the customer had acknowledged that there had been problems on its side and were willing to be more generous in their contract terms and in terms of scope going forwards. So, the first deliveries would be of existing software, which would reduce the delivery risk. Revised figures were therefore now being put forward for approval . There had initially been some concerns over cashflow which had been discussed, but that had now been significantly improved as a result of further concessions from the customer, including some advance payments. Cerner had also helped. Being late did not, of course, help on cashflow overall. But there was now more clarity in the project, risks had been dealt with and there was a better chance of delivery. The aim now was to sign as soon as possible and get on with the project in case the internal politics at the customer changed. Returning to the subject of Cerner, Mr Courtley was happy with a meeting with its CEO and the sub-contract moved risk to Cerner (an improvement).

He added that, so far as PACS was concerned, the present contract was going very well and new opportunities were arising from it.

The Chairman observed that this opportunity to reset the NHS deal needed to be grasped quickly – the present situation was not that different to Pathway or Libra. There was political sensitivity and the customer could not risk embarrassment. A risky moment had been the change in the Minister of Health but, in fact, that change had not caused a problem. A further risk would be if the person in charge of the project moved elsewhere, so he was urging Mr Courtley (who needed no urging) to bring the matter to a conclusion as soon as possible. As for the figures, experience of these projects showed that it was impossible, over the ten years of the project life, to predict correctly the outcome, but the position usually improved once there was a good baseline. The project as it stood was acceptable, but he expected extra business to come, as with PACS. He was satisfied with the progress made and would be happy when the CCN was signed. He commended the project team for its hard work. Mr Courtley agreed and also thanked Mr Hirata and Mr Nagai for their strong support.

Mr Hirata commented that, as a result of his involvement since the negotiation stage, the NHS had been his "pet project". He believed BT and IDX had been the largest risks. It was good that FS had addressed that problem and that top management had grasped it and implemented solutions, moving away from BT and IDX. He appreciated the work involved. He hoped that the CCN would be signed soon. But risks – work packages, quality, performance, other issues – could arise with Cerner and FS must be ready for them. FJ would give help and support, if they did.

Mr Nagai added that the first milestone for the revised project would be 16 December 2005. Cerner had asked FSH to guarantee FSL's performance of its sub-contract (as, indeed, had BT under its agreement) and a request would later today be made to FSH's board, through the circulation of a written directors' resolution, for approval of that guarantee.

Mr Madarame asked about the risks involved in changing from BT/IDX to Cerner and how they would be managed. Mr Courtley said that there were risks, but the agreement by the customer to take delivery of existing software for the first few months was helpful and Cerner's well-qualified team made a lot of difference. The scale of the delivery was a big issue and the scaling up of Cerner's solution was near the top of the list of risks. But he believed FS would be able to manage the risks and that FS and Cerner had the engineers to get the job done. The Chairman added that the hospitals liked Cerner, preferring them to IDX.

MoD – DII – This job was going fairly well. EDS had agreed to occupy under-used property leased by FS at Reading, which helped in the management of the Group's property portfolio.

Post Office – Horizon Next Generation – It was necessary to wait and see the result of the present negotiation.

HMRC Integration project – The customer had decided to use the Aspire framework for the integration project for Revenue and Customs. So FS, which was sub-contractor to Capgemini on Aspire, would lose the primacy it had enjoyed on the HMCE project. Nevertheless, Mr Courtley thought that FS would not lose out either technically or financially. He thought that the strong line taken in negotiations with the customer and Capgemini would result in a net benefit for FS. The eventual integration agreement would be brought to the FSMC in due course.

Libra – This project was going well. It was now in its late stages, and performance was good, as was customer satisfaction.

Home Office – The customer had been difficult, but had been very pleased by FS's response to the terrorist incidents.

DTI – FS's financial performance needed to improve, but there was a

FUJ00003674

plan to do that.

The Chairman asked if there were any further questions. There were none.

05/26 Items for noting and questions

Major disputes – progress report **FSMC/05/26**

There were no new developments at a level causing concern. There were no questions.

HR Manpower Report **FSMC/05/27**

The Chairman commented that Mr Courtley had already covered much of this subject in his replies to earlier questions. Mr Courtley said that he would just add that the recently acquired Spanish business had many – over 500 - contractors. He would be looking at whether FS could improve profitability there by examining manpower.

Signed and sealed documents **FSMC/05/28**

The list was noted and the documents signed or executed as deeds ratified, approved and confirmed.

05/27 Any other business

Mr Nagai and Mr Allnutt explained the nature of the guarantee that FSH was proposing to grant to Cerner, after which the relevant directors' resolutions were circulated for signature.

There was no other business.

05/28 Date and location of next meeting

The next Meeting of the Committee would be held in November in Tokyo and would address, amongst other things, the Mid-term Plan.

The Chairman thanked everyone for their attendance. He felt that the Meeting had been productive.

There being no further business, the Meeting ended.

……………………………………………………………………….

Chairman