

In Strictest Confidence

**POB(99)3rd
PO99/23 to 36**

POST OFFICE BOARD

**Minutes of the meeting held on 23 March 1999
at Gatwick Mail Centre**

Present

Dr Neville Bain	Chairman
John Roberts	Chief Executive
Richard Close	Managing Director Finance
Jerry Cope	Managing Director Strategy & Personnel
Mike Kinski	Non-Executive Member
Dr John Lloyd	Non-Executive Member
Miles Templeman	Non-Executive Member
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: Bob Peale, Royal Mail Director Personnel & Employee Development, for PO99/29
 Robert Bishopp, Commercial Development Director, for PO99/30
 Rob Durrant, Counters Communications Director, for PO99/31

**MINUTES OF
PREVIOUS MEETING**

PO99/23

The Board approved the minutes of proceedings from its meeting of 15 February 1999.

**MATTERS ARISING
POB(99)13**

PO99/24

The Board noted the matters arising from the meeting of 15 February 1999

Parcelforce/Freemans (i)
PO99/13

The uncertainty around the future of Sears was likely to be resolved by Easter. In discussions with Sears' CEO, Parcelforce had been told that a business opportunity was likely whatever the outcome, although the volume of business was uncertain.

**CHAIRMAN'S
BUSINESS**

PO99/25

(i) The Chairman had four key issues that would be discussed during the course of the meeting:

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- the White Paper;
 - Horizon;
 - Hewlett Packard settlement; and
 - Shaping for Competitive Success.
- (ii) The Chairman still had concerns that across the organisation areas of inefficiency and cost remained and that the Board ought to address these 'hidden' areas to determine, in broad terms, if a financial prize could be realised. In particular he highlighted losses from vehicle damage that were self-insured and the £300million loss highlighted in the Health & Safety paper.
- (iii) Activities such as the Finance Excellence Programme (FEP) and Competitive Overhead Strategic Structure Programme (COSSP), were already streamlining some inefficient or duplicated processes and the creation of the Post Office Services Group (POSG) had also sought to rationalise some inefficient practices. An update on how these initiatives were progressing and the plans for achieving future efficiencies, including those as a result of Royal Mail's Divisional restructuring, could be presented to the Board in April. A new Managing Director of POSG had now been appointed under SCS and it would be a useful opportunity for the Board to meet and understand his priorities as well as hear from the present incumbent.

Action

Richard Close

Update the Board in April on cost reduction initiatives such as COSSP and FEP, together with the rationalisation activities underway within POSG and saving options. Both the new and the old MD POSG to attend.

CHIEF EXECUTIVE'S
REPORT POB(99)14

PO99/26

- (i) White Paper. Various drafts of the paper had been seen and reviewed by The Post Office. Two particular areas, the reduction in the Monopoly and the proposals for financing commercial developments, were of concern and would be the subject of further discussions with DTI officials. The end of March publication deadline would not be achieved, Stephen Byers, the Secretary of State, having told Parliament recently that the paper would be issued within the first six months of the year; May and June were now the most likely dates.
- (ii) Any significant reference to Counters in the White Paper would need to address both the network and Horizon and DTI officials were concerned that the White Paper would be ready for publication before the outcome of the

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Horizon review was announced.

- (iii) Shaping for Competitive Success. The top 80 managers had now been briefed and onward communication was to be cascaded down the line during the next two weeks. The first series of appointments under SCS had been announced and the 1 April implementation date of the first phase was still on track. The CWU had been appraised of the activities underway.
- (iv) Hewlett Packard. Parcelforce had agreed a payment of £3.6m in settlement for SAP implementation difficulties. This payment was not conditional on maintaining a working relationship with HP.
- (v) Royal Mail Pricing. The Secretary of State had agreed Royal Mail's pricing proposals and rejected POUNC's recommendation to reduce higher weight Second Class prices and delay Presstream increases by 12 months. Royal Mail would discuss with POUNC proposals on compensation payments around lost mail.
- (vi) Pay. Authority for employee pay awards was required from DTI. The pay review for middle and junior managers within Counters was due on 1 April and a settlement up to a ceiling of x% on total pay bill would be sought. In approaching the DTI for authority it was proposed that a ceiling of y% be sought but that authorisation to use this additional amount be reserved to the Chairman and Chief Executive.
- (vii) Communications Review. An interim report had confirmed that savings of over £3m were achievable in the communications budget for 1999-00. Under the proposals staff savings of 220 posts were envisaged and it was uncertain whether reductions would be achieved on a purely voluntary basis. Both SCS and COSSP would impact upon staff numbers and it was increasingly likely that in the light of these initiatives The Post Office's redundancy policy would have to be reviewed.
- (viii) Horizon. A proposal to continue the Horizon project had been produced by Treasury following discussions with ICL. The basis of the proposal to replace the Benefits Payment Card with a Post Office benefit account into which the Benefits Agency would transfer money by ACT. Strategically the proposal was attractive but the longer term financial impact had yet to be assessed. A final report on the proposal was due with the Prime Minister by the end of April.

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- (ix) The DTI maintained their support for The Post Office although the DSS were pressing for the most cost effective solution. Treasury continued to take the lead role in developing the final report.
- (x) Financial risk remained pervasive although The Post Office had made it clear to Stephen Byers that an uncommercial proposal would not be acceptable
- (xi) ICL and its senior executives remained in a precarious position and it was difficult to see how the company could survive should Horizon fail.
- (xii) Counters had for sometime been developing contingency arrangements to deal with alternative Horizon scenarios but it remained clear that whatever the outcome some form of automation was strategically crucial to the business.
- (xiii) At this stage it was neither financially nor strategically sensible to 'moth ball' activities on the project.
- (xiv) The National Audit Office would almost certainly review Horizon and whilst The Post Office could not be investigated by the NAO, it was important to ensure that its reservations and concerns, particularly with regard to Corporate Governance, had been accurately recorded.
- (xv) The history of the project was complex and it was important that Board Members, particularly Non-Executives, were familiar with the key issues and events. A short chronological brief which summarised events would be helpful in this regard.

Agreed that the negotiating remit sought from the DTI for both the POCL and Royal Mail 1 April pay award should be y%.

Action
Stuart Sweetman

- (i) Circulate a short chronological brief to Members which set out the key events and issues that had occurred during the course of the Horizon project.

Richard Close

- (ii) Allow time at the April meeting to focus on the substance behind the statistical information reported within the Annex to the Chief Executive's report.

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OVERVIEW****PO99/27**

- (i) Profit for February was:
 - Royal Mail £24m
 - Parcelforce £(1)m
 - Counters £(5)m
- (ii) The current full year profit forecasts were:
 - Royal Mail £484m
 - Parcelforce £(20)m
 - Counters £38m
 - Post Office Group £608m
- (iii) The increase in Royal Mail's profit forecast was a result of forecast expenditure on REIMS not materialising and one-off pensions benefits.
- (iv) Operational costs in Royal Mail continued above budget with the cumulative position £112m worse than budget. It was important that Royal Mail reversed this adverse trend when entering the 1999-00 financial year.
- (v) Risk continued to outweigh opportunities within Parcelforce and whilst the full year forecast loss of £20m was being maintained, a further £4m loss was a real possibility.
- (vi) In the past two weeks Parcelforce had recovered £4.5m in outstanding debt. Debts of £1.8m still remained in the over 360 day category and this would almost certainly have to be written off within the full year accounts. Debts of £50m had been recorded last year which compared with £60.2m forecast for this year.
- (vii) A number of year end audit issues had been resolved with Ernst & Young including confirmation that Parcelforce need not write down fixed assets to the Profit & Loss account and in principle agreement to the re-living of computer equipment. The level of bad debt write-off remained a concern.
- (viii) Counters' £5m loss in February was in line with expectation, and achievement of the full year forecast was not in doubt.
- (ix) The full year Capital Expenditure forecast of £511m, was just £14m below budget with actual spend mirroring that forecast.
- (x) The EFL was currently forecast to achieve the £310m target with the £64m shortfall reported in February largely

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eliminated through improvements in working capital, but achievement would be close run.

- (xi) The post-completion audit for German Parcel would be completed in the next few days and provisional indications were encouraging. Controls over cash and banking operations were now in place. Operationally, volumes were 7% higher than last year.
- (xii) The German CEO was currently considering the make up of German Parcel's supervisory Board and in particular the possible recruitment of some of the owners of the former franchisees.
- (xiii) It was agreed that Richard Close would report to the DTI forecast outturns of:
 - Royal Mail £478m
 - Parcelforce Worldwide £(20)m
 - Counters £35m

Action

Jerry Cope

- (i) Update the Board in April on the ongoing strategic development of German Parcel.

**POST OFFICE
GROUP - 1999-2000
BUDGET POB(99)16**

PO99/28

- (i) The integrated plans and budgets had been reviewed and endorsed by Group Executive POEC members. The process was iterative with Businesses refining strategies and numbers as reviews were progressed. This particular budget round had proved difficult given the impact of SCS, German Parcel and uncertainty around the EFL flowthrough into 1999-00. It was important to maintain a cost cutting culture through firm leadership and ownership of budgets.
- (ii) The key issues for 1999-00 had been identified as being:
 - implementing SCS whilst maintaining 'business as usual';
 - development of German Parcel;
 - Horizon;
 - Royal Mail's proposed growth above GVA(L);
 - Productivity - realising the expected benefits;
 - Industrial relations; and
 - closing the existing EFL 'gap'.
- (iii) Business budgets for 1999-00 were:
 - Royal Mail £480m
 - Parcelforce £(13)m
 - Counters £31m

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- SSL £2m
- POSG £1m
- Post Office Group £571m

Group profit after tax was budgeted at £368m against a Government target of £360m. The Government target for EFL was £70m.

- (iv) Commercially the challenge for the organisation was to manage the tensions that would result from gearing up for greater competition whilst ensuring targets were achieved during a period of major change.
- (v) Three issues existed within Royal Mail's budget: volume and revenue projections, achievement of productivity and efficiency improvements and the reduction of overheads. The 12 month growth figure for National was aggressive and substantially above GVA(L), although a number of one-off activities, e.g. Royal Wedding, millennium, the introduction of ISAs, telephone code changes and pension changes, would bring significant traffic increases.
- (vi) Considerable savings from the 1998-99 forecast had been budgeted in 1999-00, although the £50m forecast from accelerating implementation of SCS was considered optimistic. A more realistic estimate was between £20 and £30m.
- (vii) Parcelforce's 1999-00 budget would be affected by any increase in the 1998-99 full year loss over and above the £(20)m currently forecast.
- (viii) Improving income was Parcelforce's main challenge and in particular maintaining the upward trend in the Next Day market which was currently relatively static.
- (ix) Counters faced three key issues in the coming year: maintaining 'business as usual' in the first year of its new vision, the roll out of Horizon and related automation projects, and delivering efficiency improvements.
- (x) The budget had been prepared on the basis that Horizon would proceed to plan and without further delay or loss of value to the business.
- (xi) Although Counters' budgeted profit target was less than that achieved in 1998-99, it had to be remembered that historically actual growth in the business was small and a significant proportion of the full year profit was from interest. The current performance was also skewed through savings realised as a result of delays in the

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Horizon project. During the course of the coming year it may prove necessary for the Board to review and agree an alternative more appropriate profit figure which allowed greater investment in the Business.

- (xii) The Business budgets resulted in an EFL 'gap' of £166m and this would be closed through activities including:
- vehicle leasing;
 - WAND financing;
 - Girobank income; and
 - working capital

noted further that

- (xiii) The underlying profitability of the Group was £222m, which, for the organisation to compete in an increasingly competitive environment, would have to be improved.
- (xiv) Royal Mail's volume growth was considered by some Members as 'bullish' and the business's ability to translate this growth into income of £199m whilst increasing manpower was questioned.
- (xv) Improved utilisation of labour and the introduction of the performance bonus scheme would drive out excessive levels of overtime and thereby improve productivity. Increases in manpower were related to delivery where quality of service and achievement of the 0930 delivery standard had to be maintained whilst volumes increased. The increase in front line staff could actually have positive consequences for industrial relations.
- (xvi) The requirement for internal consultants, of which there were significant numbers, was an issue Royal Mail would be addressing.
- (xvii) Royal Mail's risks and opportunities were balanced at slightly over £110m, and were considered manageable.
- (xviii) Crown office conversions had been factored into the budget with operational costs of £2-3m included.
- (xix) The leasing of vehicles rather than outright purchase was only being adopted to provide an EFL benefit. Price advantages similar to those realised through the business's normal bulk purchasing would be sought from the manufacturer.
- (xx) Government had agreed that the costs associated with SCS would be neutral against the Group profit target.

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(xxi) Approved the budgets and targets for 1999-00 and the actions to close the EFL 'gap'.

(xxii) Agreed that the budgets should be recast, within the overall amounts set out in the paper, as reorganisation was implemented in 1999-00.

Action

Jerry Cope

(i) Circulate a note clarifying the manpower movements in Royal Mail and in particular the use of internal consultants.

ROYAL MAIL
INDUSTRIAL
RELATIONS &
BUSINESS
PERFORMANCE
POB(99)15

PO99/29

(i) Royal Mail had worked hard over the previous three years to recover from the Employee Agenda (EA) negotiations which had resulted in severe industrial relations difficulties (PO95/26). Relations with the union over the past 12 months had improved considerably and the development and implementation of a number of new working practices had successfully been introduced. These included a:

- Conduct and attendance agreement;
- Interim delivery agreement;
- Performance bonus scheme

(ii) Two elements of the original Employee Agenda package, updated to reflect a greater emphasis on customer need, had still to be introduced. The first was the Way of Working package, which moved away from the Employee Agenda revolutionary approach based on teamworking, to an evolutionary approach based on:

- joint management/union/employee involvement in changes to work practices;
- work time learning and team briefing;
- measurement and display in work areas; and
- a joint business and commercial literacy campaign.

(iii) The final element to be agreed was on Pay and Conditions and incorporated a shorter working week, meal relief harmonisation and the introduction of a unigrade postal worker.

(iv) Negotiations were currently underway on these remaining agreements and whilst not without risk, Royal Mail's negotiating team were optimistic that agreement could be reached. It was recognised that key to the success of

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these agreements was management's implementation and ongoing monitoring of them, something that in the past had not always been successful. To reduce this risk a dedicated team of 1,000 managers working together with the CWU would be employed on implementation.

- (v) In contrast to the Employee Agenda, the CWU Executive were generally supportive of the packages being introduced and crucially had the capability of gaining employee support. A satisfactory agreement had now been negotiated at the troublesome Princess Royal Distribution Centre.
- (vi) Under the shorter working week front line employees' gross hours would reduce from 41 to 39.5 hours.
- (vii) Communicating why change was needed would as always be essential and it was important to ensure that working with the union, only one agreed communications message was issued.
- (viii) Progress with work time learning would not be contingent on implementation of the rest of the package.
- (ix) Capability to deliver change was important at all levels and ensuring the selection and appointment of appropriate individuals would not only improve the chances of success, but would also have the added benefit of improving employee motivation.

Thanked Bob Peaple and the Royal Mail Personnel team for their excellent work.

REGULATION -
STATE OF
READINESS IN THE
POST OFFICE
POB(99)17

PO99/30

- (i) The Post Office could currently take advantage of a regulator not yet being established by taking the lead in seeking to 'persuade' the incoming appointee of The Post Office's view of the market and commercial strategy. This was a process successfully exploited by Deutsche Post.
- (ii) Some processes had already been developed to deal with regulation and a single point of focus had been established into which expertise would be directed. An education programme for employees was also being developed.
- (iii) Which ever system of regulation was introduced it would

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have, from a Post Office perspective, to be subject to certain underlying principles. These were:

- the price cap (RPI-x) must be consistent with the Government set profit target;
- the uniform tariff obligation must be clearly defined;
- the roles of POUNC and the regulator must be clearly set out; and
- the regulator's scope must be limited to postal services provided under the USO.

- (iv) DTI had indicated that the regulator would be modelled on OFTEL, OFFER and OFGAS and work on these models had been undertaken. However, given that ultimately The Post Office would still operate a regulated and non-regulated business it was also sensible to study the model used by the water industry, OFWAT.

Noted further that

- (v) Given the importance of the pricing regime, it was essential that sufficient focus was put into establishing separate accounts for monopoly and non-monopoly streams. This was an area in which more work was needed and Ernst & Young were due to complete in July a review of what still needed to be done. Improved cost and contribution analysis was needed in many key areas and the Ernst & Young review would helpfully inform what further work The Post Office needed to carry out.
- (vi) Pressure to open up the network to competitors was almost certain and work on access pricing was fairly well developed.
- (vii) Informal indications from the DTI were that the initial staffing level of the regulator's office would be 44 people. Cost for this would be borne by The Post Office.
- (viii) European liberalisation would have an impact on The Post Office and it was important that the DTI did not press ahead too quickly with initiatives which might ultimately go beyond the measures introduced through EU legislation.
- (ix) The positive aspects of regulation should not be discounted, particularly the service benefits that customers would expect to enjoy.
- (x) The Post Office would be the most labour intensive organisation to be regulated and the regulator would need to understand why significant reductions in manpower were not a realistic possibility.

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- (xi) Agreed the approach to regulation that was being developed.
- Action
Jerry Cope (i) Consider more fully the OFWAT model of regulation.
- DEVELOPMENT OF A
NEW SOCIAL POLICY
FOR THE POST
OFFICE POB(99)18 PO99/31
- (i) The paper represented the first output from the review of Social Policy as applied across The Post Office and made recommendations specifically on the management of charitable giving.
- (ii) The current approach to charitable giving had no clear link to The Post Office's Purpose Direction and Values (PDV), and each business pursued its own initiatives in an ad-hoc and unco-ordinated way. Historically, The Post Office had adopted a philanthropic approach to charitable giving and a key aim of the social policy review was to move progressively away from this approach to one that established a framework of social policy building on charitable giving, community investment, commercial partnerships and basic business responsibility. Four underlying principles had been developed to support the new purpose and approach: initiatives must be anchored by The Post Office's PDV; they had to be applied consistently across The Post Office; employee and agent involvement in community affairs should be supported; and activities had to be measurable.
- (iii) Education currently accounted for 70% of the £2m budget and it was relatively easy for applicants seeking funds to make some form of link to educational issues. A much tighter set of definitions of what would be supported was required and three broad areas had been identified: People, Business and Community, all of which were interconnected. Under the banner of these themes, five Group-wide themes had been developed which would:
 - connect 'People'
 - using the written word through education
 - using technology through education
 - connect (small) businesses
 - with their customers in the community
 - connect local communities
 - by bringing them closer together and helping sustain them

connect people, businesses and the community to those entering the world of work (especially the disabled).

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- (iv) Many of the applications received for funding did not relate to The Post Office themes and this work, which tended to be reactive, accounted for a great deal of time and effort. A more professional, streamlined approach could be achieved through the introduction of a 'tendering' based process under which our support for a particular activity would be advertised and organisations invited to tender for our support. Additionally, a one stop shop for applications, possibly located within the voluntary sector, was recommended, supported by the establishment of an applications database. A focused publicity campaign which promoted the new approach was also recommended. Activities would be monitored and the results measurable.

Noted further that

- (v) External research indicated that public opinion of what themes organisations should be supporting mirrored those being proposed.
- (vi) The tendering approach had been seen to operate well for Barclays and provided a clear focus for external organisations, schools etc, of just what The Post Office supported.
- (vii) The Post Office was viewed as a benchmark for other companies and the implementation of the Social Policy was seen as the first step to further enhance this reputation.
- (viii) Employee secondments provided an important development opportunity and within Counters graduates were being given a six month posting within a charitable organisation.
- (ix) Agreed that the Social Policy would draw directly upon the PDV and that the themes would be as described in paragraph (iii) above.
- (x) Agreed that a tender based approach should be trailed, that steps to establish a 'one-stop' shop for applications for charitable support should be taken, and that consideration should be given to this being within the voluntary sector.

AUDIT COMMITTEE
REPORT POB(99)19x

PO99/32

- (i) The Board sought reassurance that progress on the Birmingham accommodation project was being

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maintained.

- (ii) Action to improve the financial controls within Royal Mail National was being progressed.
- (iii) It would be helpful if future reports could highlight those issues that the Board needed to pay specific attention to.
- (iv) The Committee wished to see an analysis of the amount being spent with external consultants.

Action
Richard Close

- (i) Update the Board via Matters Arising on the progress made with the Birmingham Accommodation project.

Rosemary Thorne

- (ii) The Committee should in future highlight those issues that the Board should pay specific attention to.

**POPS 7th
SUPPLEMENTAL
DEED & POSSS 28th
SUPPLEMENTAL
DEED POB(99)20x**

PO99/33

- (i) Agreed that the POPS 7th Supplemental Deed and the POSSS 28th Supplemental Deed could be executed.

**HEALTH & SAFETY
MANAGEMENT
POB(99)21x**

PO99/34

- (i) The work carried out under the review and the recommendations that had been made were noted

Action
Jerry Cope

- (i) Circulate information on the legal costs associated with the defence of compensation claims.

**APPOINTMENT OF A
DIRECTOR TO
ROYAL MAIL US INC.
POB(99)22x**

PO99/35

- (i) noted that Chris Powell resigned from the Board of Royal Mail US Inc. with immediate effect.
- (ii) Agreed that David Walker be appointed a Director of Royal Mail US Inc. with immediate effect.

**DATE OF NEXT
MEETING**

PO99/36

Scheduled for 27 April 1999 at 148 Old Street.