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POB(99)5th
PO99/53POST OFFICE BOARD

Minutes of the Meeting of the Board held
at 10 Courtney Place, Cobham, Surrey, at 7.30pm on Sunday
23 May 1999

Present

Neville Bain	Chairman
John Roberts	Chief Executive
Richard Close	Managing Director Finance
Jerry Cope	Managing Director Strategy & Personnel

Present by conference phone facility from 8.00pm:

Mike Kinski	Non-Executive
Rosemary Thorne	Non-Executive
Miles Templeman	Non-Executive

Also Present

Stuart Sweetman	Managing Director Post Office Counters Limited
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Apology John Lloyd was unable to attend.

HORIZON

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- (i) The Chairman noted that a quorum was present and that the purpose of the meeting was to consider the request from Government that the Post Office Board sign the Heads of Agreement negotiated by the Treasury with ICL (and to which POCL had not been party) by the ICL/Fujitsu deadline of midnight.
- (ii) It was noted that the Secretary of State had, on 22 May, finally provided a written response to the Chairman, clarifying certain aspects of the proposal. In particular the letter (attached to this minute) made plain that it is Government's desire to pursue option B3 and that all other alternatives, except for termination were off the table. The following comfort was given:
- the timing of the Benefits Agency move to Automated Credit Transfer (ACT) would not start before 2003

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- the Government would fund the £480m which POCL would require to pay ICL on the scheduled basis
- that Ministers have "hopes" that The Post Office Network would be utilised by Government departments to deliver the benefits on the 'Modernising Government' White Paper.

- (iii) This proposal was then fully discussed, and clarified to the extent possible, under the following headings:

Commercial Issues

- (iv) It was clear that there was insufficient information in the document negotiated by the Treasury, and commended to the Board by the Secretary of State, to enable a full financial evaluation to be carried out. On the limited evidence available it appeared to be around £700m NPV adverse to option A, but was still slightly superior to termination.
- (v) While in normal circumstances this would lead the Board to reject the B3 proposal on commercial grounds, it was clear that the shareholder favoured it, no other options (apart from forced termination) were available and that Government, as a customer, remained essential to POCL as a key driver of future volume.
- (vi) The proposal to take 3 months to turn the Heads of Agreement into a real agreement could be used to produce a full commercial evaluation which the Board could then, if necessary, and appropriate, reject at a cost of a £150m payment to ICL.

Funding

- (vii) It was noted that the £480m of development funding proposed by Government offset the staged payment due to ICL. It appeared that a further £68m payment for the core system would be left to POCL along with annual running costs of around £80m.
- (viii) It was noted that, as the vehicle for funding would be the sale of gilts, approximately £25m of foregone interest would impact the Post Office cash flow and bottom line.
- (ix) It was further noted that POCL would in addition

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need to fund the Banking development, not covered within the ICL payments, which would result in a further cash requirement of £100m.

Risks

- (x) It was noted that a significant risk transfer from ICL to POCL was included in the Secretary of State's proposal.

Impact on POCL Strategy

- (xi) It was noted that, apart from termination, this was the least beneficial option for Counters' strategy. However, it did provide for automation, it accelerated Network Banking requirements, that there was no migration to a Smart Card and that Government Gateway was much harder. As it was the only option Government were prepared to support, there was merit in taking time to evaluate it further.

ICL Capability and Relationships

- (xii) Despite the uncertainty and the difficulties caused by Governments intransigence, relations with ICL and POCL were professional and satisfactory. There were some concerns about their ability to deliver, which would be addressed in the next 3 months should the Board decide to proceed to sign the draft binding heads of agreement.

White Paper

- (xiii) It was an absolute essential requirement of the Board that any Horizon proposals should not impact on the funding and other aspects of the White Paper.
- (xiv) The Chairman, with the agreement of the Board, then outlined the two alternatives to be considered:
1. Refuse to sign as there is insufficient information at this time, and the evidence available suggests that the proposal is not necessarily in the best commercial interests of The Post Office.
 2. Sign subject to seeking substantial comfort from Government to protect The Post Office and POCL financial positions.

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After considerable discussion, the Board were unanimous in empowering the Chairman to speak with the Secretary of State and to confirm in writing the following:

- based on the information currently available to the Board, and bearing in mind its fiduciary responsibilities, option B3 is likely to lead to a deterioration in the financial position of The Post Office, and is not the best use of shareholder funds.
- however, the Government had made it clear that it believed it is the best way forward and The Post Office did have the opportunity of the next three months to fully understand the proposal and see if it can be made workable.
- in the light of this, the Board would be prepared to sign the Heads of Agreement to meet the deadline on the following conditions:
 - ◇ while The Post Office will work positively to create a success of the option, if the three months show this is not possible, or the performance of ICL causes further doubt about their ability to complete their part of the deal, then the £150m cancellation payment should be treated by Government in the same way as the £480m
 - ◇ in the case of both figures appropriate profit target and EFL reductions would be made and payment is made in a way that POCL ensures remains solvent and able to pay its creditors as they fall due.
 - ◇ that none of the figures mentioned in the Secretary of State's letter will in any way affect the proposals, including funding for acquisitions so far put forward in the Government approach to the White Paper
 - ◇ that because POCL is largely exempt from VAT, Government will ensure that the VAT effects on the payments to ICL are neutral to The Post Office.

The Board also registered its deep concern about the way in which this issue has been handled and about the relationship between the Secretary of State and the Board. It therefore required an urgent meeting between The Chairman the non-executives and the Secretary of State.

- (xv) The Board agreed that subject to a satisfactory response to the issues listed above, that a Committee of any three of the Board, including the Chairman and

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the CEO and one other, should be empowered to agree that Stuart Sweetman sign the draft heads of agreement.

- (xvi) Note: Subsequent to the formal meeting the Chairman fully reviewed the process, the facts and the discussion with Dr John Lloyd who also had received all briefing papers. Dr Lloyd wishes to record that he is in full agreement with each and every aspect of the conclusion and joins completely in the decision of the Board.