

In Strictest Confidence

POLB(06)6th
POLB 06/79 – 06/98

Post Office Limited

(company no. 2154540)

Minutes of the meeting of the Board
held at 148 Old Street, London
on October 26th 2006

Present:

Sir Michael Hodgkinson	Chairman, Post Office Limited
Ian Anderson	Human Resources Director
Alan Cook	Managing Director
Peter Corbett	Finance Director
David Glynn	Sales Director

In attendance:

Crispin Beale	Director of Customer Insight, Intelligence & Analysis
Richard Barker	Acting Network Director
Rob Durrant	Programme Office Director
David Smith	IT Delivery Director
Neil Owen	Notes

Apologies:

Adam Crozier	Chief Executive, Royal Mail Group
Jonathan Evans	Company Secretary
Ric Francis	Operations Director
Allan Leighton	Chairman, Royal Mail Group
Sue Whalley	Strategy Director

POLB06/79 MINUTES OF PREVIOUS MEETINGS POLB(06)4TH + 5TH

- (a) The Board approved the minutes of the Board meetings of June 28th 2006 and September 27th 2006.

POLB06/80 MINUTES FOR NOTING

- (a) The Board noted the minutes of the Post Office Ltd Executive Team meeting of 14th September and the Investment Committee of 13th October 2006;
- (b) the Board noted the minutes of the First Rate Exchange Services Ltd Board meeting of 23rd August 2006;
- (c) the Board noted the minutes of the POFS Board meeting of 28th September 2006;

POLB06/81 RESIGNATION AND APPOINTMENT OF DIRECTORS

- (a) The Chairman reported that the appointment to the Board of

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David Glynn had been approved by the Royal Mail Holdings Nominations Committee, and his appointment would be effective from 26th October 2006.

- (b) the Chairman reported that the appointment to the Board of Gary Hockey-Morley had been approved by the Royal Mail Holdings Nominations Committee, and his appointment would be effective from 30th October 2006.

POLB06/82 STATUS REPORT POLB(06)51

- (a) The Board noted the report, and that all actions had been completed. In addition the Board noted that:
- (b) Luke March, Compliance Director Royal Mail Group had agreed to join Post Office Ltd's Compliance Committee, and was now receiving formal invites to each meeting;
- (c) Crispin Beale clarified that the CSI proposal had now been discussed at the Remuneration Committee and that this action was now closed.

POLB06/83 CHAIRMAN'S BUSINESS

- (a) Sir Michael Hodgkinson reported the following matters to the Board:
- (b) the strategic plan, together with the options for reshaping the network, had been well received by both the Royal Mail Holdings Board and Government. The outcome of the Government's decision concerning network numbers, together with the start date for consultations on any closures, had been deferred. Alan Cook stated that the likely earliest date for a decision was now the third week in November. Mike Hodgkinson pointed out that once a decision had been reached the Board should expect another two-stage approach consisting of an overarching principal, followed by more detailed 'small print';
- (c) Peter Corbett informed the Board that a large number of different network scenarios had been modelled over the last few weeks. One of the key issues that had emerged was whether urban and rural branches which could only break even would form part of the rationalisation programme. Other issues included devising a strategy to deal with *force majeure* closures and formulating an appropriate funding mechanism to increase the number of counter positions in receiving branches. There was also a good case to amend the compensation scheme and make more use of POL Lite;
- (d) Mike Hodgkinson stated that a need existed for the Post Office to help the Government with their methodology for constructing a detailed framework. Considerable effort

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- would need to be made to ensure the wording of any such scheme was appropriate to the needs of the business.
- (e) Alan Cook reported that a new manager had now been recruited to manage the community network and help provide it with its own identity. Nevertheless there were considerable difficulties in effectively 're-launching' POL whilst simultaneously closing branches. An attempt by Natwest to undertake a similar exercise in the 1990s had proved very damaging to them. The press had recently focused their attention on Government, but this would soon shift back to POL particularly if there was a further roll-out of WH Smith branches.

POLB06/84

MANAGING DIRECTOR'S REPORT

- (a) Alan Cook explained that the Top 50 managers had been briefed successfully on the strategic plan, and the next stage would be to brief 1000 managers in two large tranches of 500. The plan now had additional credibility given what had been achieved over the previous three years;
- (b) negotiations continued to ensure Card Account customers remained with POL. Current thinking was that the top one million customers would be offered savings account, one million would migrate to the banks, and two million may stay on with a new Card Account product with a different price and functionality. Although the Card Account option would earn POL less money, it would help prevent a total loss of business;
- (c) the Executive Team had agreed to abide by the voluntary Banking Code Standards Board;
- (d) under the revised system of delegated authorities, Post Office Ltd was holding its own Investment Committee meetings twice a month to consider investment cases;
- (e) a trial roll-out of the car insurance 'quote and sale' system was underway in 35 branches. Mike Hodgkinson informed the Board that the Group Audit Committee's main concern had been about the sales of 'financial advice' products. Therefore the Royal Mail Holdings Board is required to approve all new POL products to protect the brand by ensuring any new products launched were both within the capability of its sales force and followed the principal of being simple, good value products;
- (f) progress on commitments to Ofcom regarding mis-selling has been good and all actions had or would be delivered by the end of October. Figures for September showed a slight improvement and it was expected that October would show the benefit of remedial measures in both branch and field sales. The measures were expected to deter mis-selling, but the risk remained that by mid-November the impact may not

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convince Ofcom that the root causes had been addressed and thereby trigger a formal investigation. Ofcom had also been informed that new codes of practice concerning information to be given to customers on premium rate and other services had not been put in place, as required by a change to their rules that came into effect in August. This oversight has identified a weakness in the current reliance on suppliers to inform POL of new requirements [REDACTED]

[REDACTED] The problem identified with the telephony products in respect of the Code of Practice was being addressed, although this would take 6-8 weeks because of the logistics of getting new documents printed and circulated to branches. It was agreed that [REDACTED]

ACTION:
Crispin Beale

and the matter would be discussed further at the next Risk and Compliance Committee meeting.

POLB06/85

FINANCE REPORT POLB(06)52A

- (a) Peter Corbett provided the Board with a presentation on the Period 6 business performance results;
- (b) income was £14.2m lower than budget due to lower than expected HomePhone and retail sales;
- (c) a new forecast had been submitted to Group Finance which showed that Post Office Limited would achieve its full year loss target but by means of significant cost reductions to counter a significant revenue decrease. This latest forecast also included the £20m expenditure challenge as part of the cost savings. The new company structure was now in place and budgets had been reissued. The cost savings had been partly achieved by making budget reductions as part of this process. No savings were planned from the £20m "transformational pot" – although recent decisions around Field Sales and McKinsey costs had affected the proposed usage of the pot, so further consideration of how these funds were utilised was required;
- (d) Ernst and Young had conducted their review of Post Office Ltd's half year financial performance. The review concluded without incident, and progress was demonstrated against all management letter points from last year. An update to the Audit and Risk Committee in respect of the IMPACT housekeeping exercise had been prepared to demonstrate the progress that had been made. Ernst and Young had been requested to perform a limited scope audit of POLFS during Period 8 to highlight further progress as the full audit at year end approached. It was possible that before year end some of the provision made in the accounts last year in respect of the IMPACT balances may be written back, but further analysis was needed to be certain of this and

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quantify any write back amount.

POLB06/86

SOLVENCY AND FUNDING STATUS

- (a) As referred to in the MD's report, there had been intense activity in modelling various network scenarios since the last Board meeting and a letter had been sent to Stephen Lovegrove;
- (b) based on the discussions that had taken place with the DTI and Treasury, the Board continued to have confidence that the funding issue would be dealt with prior to the end of December 2006;
- (c) it was agreed that the funding position and going concern status would be reviewed and agreed at each meeting;

ACTION:
Peter Corbett

POLB06/87

**RAPID RATIONALISATION OF POST OFFICE LTD
POLB(06)52B**

- (a) Peter Corbett presented a paper that outlined in detail the necessary actions which would need to be taken if further funding was not forthcoming. There would have to be a rapid rationalisation of the organisation, including a reduction in the agency network to 3,000 offices, a reduction in the Directly Managed network to 100 branches, a reduction in central costs and the sale of assets. Currently there was sufficient funding in place for Post Office Ltd to trade until March 2008 on a "manage for cash" basis. However these funds did not allow for any investment in the Commercial segment so the rationalisation would need to start earlier than March 2008 to produce savings because the Commercial segment could not afford to "tread water" until March 2008;
- (b) the Board noted the paper and agreed that refinement was required in certain areas. It was also agreed that further iterations of the paper would be reviewed at each subsequent ET meeting.

ACTION:
Peter Corbett

OTHER EXECUTIVE REPORTS

POLB06/88

NETWORK REPORT POLB(06)53

- (a) - The Board noted the report, and also noted that:
- (b) VR: detailed arrangements for VR had been deployed at local level for Managers in Directly Managed network and around 100 managers would be provided with a formal offer;
- (c) WH Smith: five of the six pilot branches had now opened and these had been visited by the members of the WH Smith Board. Their assessment of the integration had been positive, and they had expressed a willingness to proceed

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with further initiatives. Huge efforts had been made by WH Smith to improve sales at Post Office branches, and although this was going well, FRTS had noted that bureau sales have been affected. Alan Cook reminded the Board that this was a pilot scheme which would only be taken further should the trial be shown to provide a clear benefit to Post Office Ltd. Further discussions would take place with Kate Swan from WH Smiths;

- (d) Commercial: sales targets and scorecard measures had been issued to all new Heads of Business Development and their teams. The sales focus was on closing the current income gap by concentrating on Travel products, Credit Card, Car Insurance and Home Insurance;
- (e) Agency Development: terms of reference had been developed for the agents' remuneration review and project planning underway. The first programme team meeting had taken place on 18th October 2006;
- (f) Community: a customer measure would be developed for the top 1550 branches identified as having the highest sales potential.

POLB06/89**OPERATIONS POLB(06)54**

- (a) The Board noted the report and in particular that:
- (b) Stock Programme: the physical move of the stock centre from Hemel to Swindon had taken place. Full order processing was now taking place from Swindon, but there were significant problems. Alan Cook emphasised that this shared service with Royal Mail was critical to Post Office Limited, and subpostmasters had continued to raise a large number of issues. It was agreed that the matter would be raised at the Royal Mail Holdings Board;
- (c) Horizon Next Generation: the Horizon Next Generation contract was signed with Fujitsu Services in September. This contract would provide Post Office Limited with the platform to increase delivery capability at significantly reduced costs.

**ACTION:
Alan Cook****POLB06/90****PEOPLE & ORGANISATIONAL DEVELOPMENT
POLB(06)55**

- (a) The Board noted the report and in particular that:
- (b) Age Discrimination Legislation: discussions with the CWU over the last year had failed to reach agreement on ceasing the practice of using seniority as the basis for annual leave selection.

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October the CWU were formally notified that seniority would no longer be used for annual leave allocation and a new rotational system had been circulated to DMB's and Cash Centres. The CWU had not yet formally responded but local representatives had instructed their members not to sign for annual leave (from April 2007) on a rotational basis;

- (c) Have Your Say: I enjoy working here was 59% for September and around 60% year to date, although this had fallen from 64% at the same time last year. I feel this company values me is 28% for September and 27% year to date, again down compared to the same time last year when it was 33%. Response rates continued at 73% for September, compared to 53% last year. Those attending a WTL session were higher than last year at 71% year to date but only 56% were finding them useful and this was down slightly on last year. 48% had seen an improvement since the last opinion survey, a similar result to this time last year at 49%;
- (d) Pay Deal: the CWU pay deal had been agreed at ballot and implemented in September. The CMA pay deal had been agreed at 3.15% (for 11 months) effective 1st July. Subject to Yes ballot, it would be paid (with backdating) in December;
- (e) Reward Structure: a project team had been established to manage engagement with Unions, Key Group Stakeholders, Colleagues and Development & Delivery of reward activities. The Executive Team had agreed an approach to recognise those with bigger roles as a result of new structural design. This would be communicated by letter at the end of October and implemented in November. The Group Executive Team had approved a Group approach for broadband structure, and there was a potential risk for POL timelines being delayed by Group.

POLB06/91**MARKETING REPORT POLB(06)56**

- (a) The Board noted the report, and in particular that:
- (b) Pricing In Proportion: customer awareness of PIP continued to increase slightly and was now at 92% among consumers. More than 60% felt they knew a lot or something about the changes. Work was currently progressing to ensure Post Office Ltd supported Royal Mail's campaign for Christmas, and there would be brochures and posters in all branches;
- (c) Telephony: Post Office® HomePhone had now signed up over 890,000 customer contracts, of which 400,000 were live making calls. Approximately 300m calls have been made since launch, generating £65m in revenue. The business was growing significantly, with 35m calls made in September alone, generating over £7m in revenue. Current

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focus was on consolidating the significant growth this year and resolving outstanding sales related compliance issues and operational difficulties that had arisen as the business has grown;

- (d) Financial Services: there were now over 670,000 POFS customers and this was growing at the rate of almost 50,000 a month. Total sales since April are 347,700. Post Office® Instant Saver accounts have reached 108,300, with balances of over £1bn which was 281% of target;
- (e) Posted Magazine: the renamed Sorted magazine had received two awards and had generated huge responses from its readership.

POLB06/92**SALES REPORT**

- (a) David Glynn provided the Board with an update;
- (b) Engagement Plan: an engagement plan had been drafted and would be presented to the Executive Team shortly for approval;
- (c) Field Sales: the decision had been made to exit field sales by November 30th 2006 because of the hidden costs of acquisition that had come to light when the issue was reviewed;
- (d) Foreign Exchange: although growth had been less than expected, the market in general had been declining. Some of the recent new entrants into the market were already experiencing declining volumes. However, Mike Hodgkinson pointed out that the supermarkets would be offering this product shortly and the situation would need to be kept under careful review.

POLB06/93**STRATEGY REPORT POLB(06)57**

- (a) An integrated 5 year strategy to transform the business had been signed off by the Holdings Board on October 3rd. High level versions had been shared with the NFSP, CWU and CMA. In addition Andy Furey had received a personal copy of the plan as part of the talks on the future of the Crown Office network. The DTI and Treasury had also been taken through the details and the implications of the strategy and plan. Communications of the strategy would take place at upcoming launch events.

POLB06/94**PROGRAMME OFFICE REPORT**

- (a) Rob Durrant provided a short update;

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- ACTION:**
Peter Corbett
- (b) the year to date headcount reduction of 670 was encouraging and suggested Post Office Limited would achieve its full year target of 1000 despite the fact that there had been fewer than expected conversions;
 - (c) a much more detailed update was being provided at the Executive Team meeting which would take place directly after the Board meeting;
 - (d) it was agreed that Peter Corbett would provide the Group Finance Director with an update to incorporate within the finance report to the Royal Mail Holdings Board to demonstrate the progress that had been made by Post Office Ltd, and the cost of delays brought about by the Government's late decision on network size.

POLB06/95**PAYSTATION BUSINESS CASE POLB(06)58**

- (a) Crispin Beale presented the Paystation business case to the Board;
- (b) approval for the extension of the Post Office paystation™ network by 3,000 terminals from 4,500 to 7,500 sites in order to grow and defend our core bill payment service, and to enable us to compete more effectively with other network providers - such as PayPoint and PAYzone. This initiative is a vital part of Post Office Ltd's Bill Payment Strategy to arrest the decline in bill payment transactions, and to become more pro-active in responding to market conditions and competitor activities;
- (c) the business case had been approved by the POL Executive Team on 26th July and Group Investment Appraisal on 22nd August 2006;
- (d) the Board agreed the business case.

POLB06/96**HEALTH & SAFETY POLB(06)59**

- (a) Ian Anderson presented a Health and Safety paper to the Board. The Board noted the report and the following matters were highlighted:
- (b) absence accidents were 25% down against 2005/06. Levels remained extremely low in the DMBs and lower than in Royal Mail Letters and Cash Services;
- (c) reportable (RIDDOR) accidents were down 20.6% on 2005/06;
- (d) days lost due to accidents (including trauma from attacks on cash in transit crews) were down 11.6% although the running rate was marginally over target. All accidents were

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down 13.1%;

- (e) Have Your Say results were at 73.4% against a target of 67% for responses to health and safety questions in the Directly Managed sector;
- (f) Branch Office Manager, Deputy Branch Manager and Cash Services Operations Manager face to face health and safety competency training had been completed;
- (g) Work Time Listen and Learn (WTLL) delivery at DMBs remained a cause for concern at 65%, although improvements had been made over 2005/06.

POLB06/97

SEALINGS POLB(06)60

- (a) The directors approved the affixing of the common seal of the Company to the documents set out against item number 110/06 and 180/06 inclusive in the seal register.

POLB06/98

CLOSE

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