



Appendix F

Extracts from 2009 contract between the United Kingdom Secretary of State for Defence and BVT Surface Fleet Ltd

This appendix supplements the Committee's comments in paragraph 2.220 in chapter two. This contract has resulted in a long-term shipbuilding partnership between the UK Ministry of Defence and BVT Surface Fleet Ltd (which has since been absorbed into BAE Systems). The most relevant pages with pertinent clauses of the contract have been extracted:

- 'Background' in clauses A to H explains that the aim of the contract is to fulfil the policy in the Defence Industrial Strategy White Paper and, to this end, BVT Surface Fleet Ltd (BVT) has been asked to create a surface ship business.
- The 'Commercial Purpose' of the contract in clause 7. This specifies what is to be provided, targets to be achieved, obligates the parties to maximise efficiencies, share information and confirms BVT's exclusive position.
- 'Exclusivity' provided in clause 9. By default, BVT is granted exclusive rights as lead contractor; however MoD makes no express commitment to procure from BVT. Exclusivity exists when the MoD selects BVT for certain naval procurements and obligations to work as partners then commence.
- 'Savings Targets' are described in clause 14. These clauses outline savings targets to be achieved.

- 'Key Industrial Capability' in clause 20. The contract explains that BVT undertakes to maintain key industrial capabilities. Certain conditions may trigger a payment from the UK MoD to support BVT sustain key industrial capabilities.

- 'Partnering' obligations are established in clause 29. The MoD and BVT agreed to collaborate and partner together and cooperate to demonstrate how individual contracts achieve value for money.

- 'Supply Chain Principles' in clause 30.6 describe how BVT should oversee and manage its supply chain.

[REDACTED] (CONTRACT NO: MCP/001)

Terms of Business Agreement relating to BVT Surface Fleet Limited and its business

**THE SECRETARY OF STATE FOR DEFENCE OF THE UNITED KINGDOM OF GREAT
BRITAIN AND NORTHERN IRELAND**

and

BVT SURFACE FLEET LIMITED

and

BAE SYSTEMS PLC

and

VT GROUP PLC

Dated

2009

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Terms of Business Agreement

Dated

2009

Between

- (1) **The Secretary of State for Defence of the United Kingdom of Great Britain and Northern Ireland** (the MoD);
- (2) **BVT Surface Fleet Limited** (Company No. 06160534) whose registered office is at Daring Building 2-166 Postal Point 100, Portsmouth Naval Base, Portsmouth, Hampshire PO1 3NJ (**BVT**);
- (3) **BAE Systems plc** (Company No. 01470151) whose registered office is at 6 Carlton Gardens, London SW1Y 5AD (**BAES**); and
- (4) **VT Group plc** (Company No. 01915771) whose registered office is at VT House, Grange Drive, Hedge End, Southampton, Hampshire SO30 2DQ (**VTG**).

Background

- A The Defence Industrial Strategy White Paper of December 2005 sets out the Government's policy for the UK's surface ships Naval Industrial Sector (the **Sector**). It called for the transformation of the Sector, for the maintenance of Sovereign Capability and for consolidation within the Sector as a means to achieve those things.
- B BVT has been established by VTG and BAES to create a surface ship business that consistently delivers the best equipment, services and support to the Royal Navy in the most cost effective and efficient manner that mutually benefits the interests of the UK Armed Forces, and the UK tax payer.
- C The MoD, BAES and VTG recorded their intention to enter into this Contract in the Heads of Terms (as defined below). This Contract replaces and extinguishes the Head of Terms and satisfies any obligation any of the Parties may have had in relation to the Heads of Terms.
- D This Contract contains commitments on the MoD's part. These are given in exchange for BVT's obligations, in particular (1) to achieve Efficiency Savings to meet the Guaranteed Minimum Target and (2) to operate its business generally in a way which is calculated continuously to deliver savings to the MoD. These matters are recorded in the Commercial Purpose provisions which are central to this Contract.
- E BVT has been established to create a world class shipbuilding and naval support business and it is the intention of BVT to make the BVT Business achieve Upper Quartile Performance by transforming and rationalising the Transferred Business in a partnering relationship with the MoD.
- F BAES and VTG are parties to this Contract for the purposes of guaranteeing the performance of BVT's obligations under this Contract and giving certain undertakings in relation to the establishment of BVT and their ongoing conduct.
- G The MoD considers that the sustainment of Sovereign Capability through the provision and maintenance of the Key Industrial Capability and any resulting KIC Payment is a measure necessary for the protection of the essential interests of the United Kingdom's security.
- H The MoD and BVT each intend this Contract and all other arrangements which form part of the MoD's maritime change programme to be consistent with each other.

Part 3 – Purpose

7 Commercial Purpose

7.1 General

The MoD and BVT shall (and BVT shall procure that each BVT Subsidiary shall) take the steps contemplated by this Contract and such other steps within their spheres of competence as shall be reasonably necessary or expedient to secure the achievement of the Commercial Purpose.

7.2 Commercial Purpose

The Commercial Purpose is that:

- (a) this Contract is performed;
- (b) the Project Contracts are managed;
- (c) the Dockyard Contracts are managed; and
- (d) BVT and each BVT Subsidiary operates across the full extent of its dealings with the MoD,

so as to secure that:

- (i) BVT shall maintain Surface Ship Capability and Key Industrial Capability in accordance with Part 7 (*Key Industrial Capability*), and MoD discharges its commitments in respect of Key Industrial Capability in Part 7 (*Key Industrial Capability*);
- (ii) the Guaranteed Minimum Target is delivered to the MoD in accordance with Part 5 (*Integration, Transformation and Strategic Rationalisation*);
- (iii) the BVT Business is transformed to achieve Upper Quartile Performance (or such other level of performance as may be agreed between the MoD and BVT) by December 2015 (measured in accordance with Clause 19 (*Continuous Improvement, Benchmarking and Upper Quartile Performance*)), subject to, where requisite to achieve this, both the MoD and BVT implementing the recommendations (or other agreed actions) arising from the Strategic Review in 2010-11 carried out in accordance with Part 11 (*Governance, Dispute Resolution and Reporting*);
- (iv)
 - (aa) the BVT Business is operated;
 - (bb) the MoD operates;
 - (cc) BVT and the MoD operate jointly;

as efficiently and economically as is reasonably possible so as to minimise the Total Cost of Services to the MoD, recognising that transformation activities will evolve over the Contract Period;

- (v) the MoD is fully and proactively informed and advised at all times by BVT of BVT's best opinion of the measures and strategic choices the MoD might take so as to minimise the Total Cost of Services;

- (vi) the MoD is fully informed and advised of the practical and cost implications of any strategic scenarios or options which it notifies BVT that it is considering from time to time; and
- (vii) BVT is afforded the degree of exclusivity on future Work provided for in accordance with Part 4 (*Exclusivity*) and Schedule 3 (*Exclusivity*).

7.3 MoD Remedy

The Parties acknowledge that any dispute arising from this Clause 7 shall not give rise to any right to terminate this Contract under Clause 39.1.4 (*material breach*) (unless in relation to a matter which is also a BVT Default pursuant to another provision of this Contract) until any dispute resolution procedure invoked as provided for at Schedule 2 (*Dispute Resolution Procedure*) has been fully exhausted and then only in the event of breach of this Clause 7 which is a material breach of this Contract.

8 Standard of conduct

8.1 General

In carrying out its obligations under this Contract, each of BVT and the MoD shall act with due efficiency and economy and in a timely manner, including in all respects with that degree of skill, diligence, prudence and foresight which should be exercised by a skilled and experienced:

- (a) shipbuilder, defence maritime engineering contractor, systems integrator and ship support contractor having the functions which BVT has (in the case of BVT); and
- (b) defence procurement agency and national ministry of defence having the functions which the MoD has (in the case of the MoD).

8.2 Consistency of approach

In particular, in taking steps to achieve the Commercial Purpose both BVT and the MoD shall use all reasonable endeavours to ensure that: all parts of their organisations; and in the case of BVT only, the organisation of each BVT Subsidiary; and every person acting on its behalf or under its authority or control (including its sub-contractors), shall establish and maintain consistency in their assessments of and dealings with subjects for their consideration and their application of, and compliance with, all Project Contracts, Dockyard Contracts and this Contract.

Part 4 – Exclusivity

9 Exclusivity

9.1 Lead Contractor

Appointment

- 9.1.1 The MoD hereby grants to BVT the exclusive right to act as the Lead Contractor and Class Output Manager, subject to Clauses 9.1.7 (*MoD Approval Process*) and 9.1.9 (*Process following negative assessment*) and (if applicable) Clause 39.4 (*Partial Termination*), for Future Naval Programmes during the Exclusivity Period on the basis specified in Schedule 3 (*Exclusivity*).

No workload commitment

- 9.1.2 Notwithstanding the provisions of Clause 9.1.1 (*Appointment*), BVT acknowledges that the MoD is under no obligation under this Contract or otherwise at any time during the Contract Period to procure or Order any Future Naval Programme or Designated Naval Vessels or Additional Vessels and may cancel an invitation to tender issued to BVT under Clause 9.1.3 (*MoD Invitation to BVT*) at any time. However in the event that the MoD does decide to procure or Order Future Naval Programmes or Designated Naval Vessels or Additional Vessels (including where such vessels have already been subject to a cancelled procurement) the provisions of this Clause 9 and Schedule 3 (*Exclusivity*) shall apply.

MoD invitation to BVT

- 9.1.3 Where during the Exclusivity Period the MoD decides to procure one or more Designated Naval Vessels within a Future Naval Programme, it shall invite BVT in writing and only BVT to tender to provide such Designated Naval Vessels in the role of Lead Contractor and/or Class Output Manager on the basis described in Schedule 3 (*Exclusivity*), subject always to Clauses 9.1.7 (*MoD Approval Process*) and 9.1.9 (*Process following negative assessment*) below. BVT and the MoD will agree in good faith a reasonable period to develop a programme for the tender and shall identify the stages and key dates in the procurement process at which Value for Money is to be measured, including a date when it is anticipated that the final Value for Money test will be undertaken by the MoD.
- 9.1.4 BVT and the MoD shall thereafter comply in all material respects with Part 8 (*Partnering*) and in progressing the development and delivery of any new work in accordance with the MoD Approval Process.

Sharing of concerns

- 9.1.5 The MoD shall ensure that where BVT has been invited to tender without competition in relation to Future Naval Programmes or Designated Naval Vessels within a Future Naval Programme the relevant MoD project teams will share with BVT and the Steering Group any concerns identified by them that the prices and solution being developed by BVT as presented to the MoD prior to submission of the formal tender response are unlikely to represent Value for Money and shall offer reasonable assistance to BVT to enable it to address any concerns.

Submission of tender

- 9.1.6 At the dates agreed between BVT and the MoD in Clause 9.1.3 (*MoD Invitation to BVT*) BVT shall be entitled to submit its tender proposals for Designated Naval Vessel(s) which shall be sufficiently detailed so as to enable the MoD to conduct any Value for Money test.

MoD Approval Process

- 9.1.7 The award of any Order or contract for the provision of any Future Naval Programme or Designated Naval Vessels pursuant to this Part 4 shall always be subject at all times to the MoD Approval Process confirming that the tender proposal submitted by BVT for the provision of the relevant Future Naval Programme or Designated Naval Vessels (whether in relation to the role of Lead Contractor or any BVT Exclusive Stages or the role of Class Output Manager) represents Value for Money. For the avoidance of doubt this is the only ground upon which the MoD may reject a tender proposal for a Future Naval Programme or for a Designated Naval Vessel provided that the MoD reserves the right to cancel the tender process for a Designated Naval Vessel or Future Naval Programme at any time without liability to any party.

Value for money assessment

- 9.1.8 In assessing whether a proposal represents Value for Money the MoD shall:
- (a) take into consideration:
 - (i) the likely cost to the MoD of procuring the Works from a competent third party with appropriate domain experience;
 - (ii) the ability to meet the MoD's full range of capability requirements (including systems integration and support);
 - (iii) the anticipated volume of workload and any relevant restrictions or constraints that BVT has with regard to infrastructure and technology in meeting the MoD's requirements; and
 - (iv) the MoD's need to sustain Sovereign Capability;
 - (b) exclude from the assessment any element of the price for the relevant Designated Naval Vessel which has been included by BVT (with the agreement of the MoD) as being in satisfaction of a sum which is properly due and payable pursuant to this Contract (for example any Actual Strategic Rationalisation Costs which BVT and the MoD have agreed will be included in any future overhead charge).

Process following negative assessment

- 9.1.9 In the event that BVT is unable to demonstrate to the MoD's satisfaction (acting reasonably) that the tender proposal submitted by BVT for all or some of the role of Lead Contractor, any role in relation to the BVT Exclusive Stages or the role of Class Output Manager in respect of any Future Naval Programme or Designated Naval Vessels delivers a solution offering Value for Money in accordance with the MoD Approval Process, the MoD shall be entitled to request tenders from competent third parties with appropriate domain experience for the role of Lead Contractor, any role in relation to the BVT Exclusive Stages or the role of Class Output Manager (as the case may be) of such Future Naval Programme or Designated Naval Vessel and any resultant contract shall be awarded based on criteria determined by the MoD at its sole discretion provided that the tender process for such contract has been conducted by the MoD in a fair and transparent manner consistent with the good procurement practice. The MoD shall not unreasonably exclude BVT from competing in this further tender process involving third parties.

Cancellation

- 9.1.10 In the event that a tender proposal is rejected even though it represents Value for Money (for example if it is decided by the MoD that the relevant Designated Naval Vessel or Future Naval Programme is unaffordable) this shall be treated as a cancellation for the purposes of Clause 9.1.2 (*No workload commitment*) and BVT shall retain exclusivity in respect of such Future Naval Programme or Designated Naval Vessel.

Awards to third parties

- 9.1.11 In the event that any contract or Order for works and services for the Designated Naval Vessels in respect of which BVT has exclusivity rights are awarded to a third party:
- (a) BVT shall be under no obligation to provide further support to such third party in the discharge of such contract other than as agreed between BVT and the MoD or other than where already contracted for a Stage; and
 - (b) BVT shall retain its rights and remedies under this Contract and the submission of a further tender or proposal by BVT pursuant to Clause 9.1.7 (*MoD Approval Process*) shall not constitute a waiver by BVT of its rights in the event that a dispute arises or has arisen as to whether BVT's initial tender submitted pursuant to Clause 9.1.7 (*MoD Approval Process*) represents Value for Money, provided however that BVT agrees that it shall not disrupt or otherwise hinder or seek an injunction or order for specific performance to stop such further tender process being conducted by the MoD; and
 - (c) the MoD shall, where a KIC Trigger Event occurs, become liable to pay the KIC Payments to BVT in accordance with Part 7 (*Key Industrial Capability*).

9.2 Miscellaneous

- 9.2.1 Where BVT receives confirmation that its tender proposal does represent Value for Money BVT and the MoD shall within a reasonable period to be agreed carry out further works to develop appropriate terms to implement the work on the terms of the tender.
- 9.2.2 Subject to Clause 9.2.1 and the obtaining of final approvals required by the MoD and BVT and agreement being reached on the contractual terms, the MoD and BVT (or a BVT Subsidiary) shall enter into a valid and legally binding contract for the Designated Naval Vessel(s).

Contents of Relevant Contracts

- 9.2.3 It is acknowledged by BVT that a contract awarded for Work on a Designated Naval Vessel or Future Naval Programme (as the case maybe) will specify the responsibilities of BVT and in circumstances where BVT's responsibility for any Stage is at variance with Clause 9.3 and Schedule 3 (*Exclusivity*) the terms of the relevant contract shall take precedence over the provisions of Clause 9.3.

9.3 Schedule 3 (Exclusivity)

Schedule 3 (*Exclusivity*) shall apply subject always to this Clause 9 (*Exclusivity*). Both the MoD and BVT shall comply with it.

Part 6 – Savings Targets, Performance Management and Incentive Payments

14 Savings Targets

14.1 Savings Targets

Establishment of targets

- 14.1.1 Whilst there is no limit on the level of Efficiency Savings that BVT and/or the MoD and/or the JPO is entitled to propose over the Contract Period, the MoD and BVT have agreed that BVT's Guaranteed Minimum Target, Intermediate Savings Target and Stretch Savings Target for the generation of Efficiency Savings against the Baseline by the fifteenth anniversary of the date of this Contract (together the **Savings Targets**) are:

Guaranteed Minimum Target: £350,000,000 (three hundred and fifty million pounds) (Indexed)

Intermediate Savings Target: £650,000,000 (six hundred and fifty million pounds) (Indexed)

Stretch Savings Target: £900,000,000 (nine hundred million pounds) (Indexed)

BVT obligations

- 14.1.2 BVT shall generate the Guaranteed Minimum Target before the end of the Initial Term. Delivered Efficiency Savings only shall count towards Savings Targets. Delivered Efficiency Savings shall be counted after deduction of Pre-April 2009 Allowable Integration Costs and Allowable Transformation Costs for the relevant Contract Year (but for the avoidance of doubt any Allowable Strategic Rationalisation Costs shall not be deducted from Delivered Efficiency Savings).
- 14.1.3 BVT shall use all reasonable endeavours to deliver to the MoD Delivered Efficiency Savings at the Intermediate Savings Target and Stretch Savings Target by the end of the Contract Period.
- 14.1.4 It is agreed that Efficiency Savings may be generated from both the BVT Cost Base and the MoD Cost Base and that, in order to achieve the Intermediate Savings Target and Stretch Savings Target, savings will need to be made through joint transformation.

BVT Overhead Baseline

- 14.1.5 The BVT Overhead Baseline (which is one of the Baselines to be utilised for the calculations in Clause 18.1 (*Savings Calculations*)) shall comply with the form containing budgeted data set out in Part 1 of Schedule 11 (*Performance Management and KPIs*). As soon as reasonably practicable after the Commencement Date, BVT and the MoD shall update this budgeted data for actual costs certified by CAAS. This updated actual costs data shall be the BVT Cost Base in relation to overheads for 2008/2009 adjusted by:

- (a) deducting any Pre-April 2009 Allowable Integration Costs which are included in the 2008/2009 costs data; and
- (b) adding Anticipated Pre-April 2009 Integration Efficiency Savings,

and following such adjustments this shall then constitute the **BVT Overhead Baseline**.

- 14.1.6 The BVT Overhead Baseline referred to in Clause 14.1.5 above shall be stored in the BEM. The JPO: (i) may adjust the BVT Overhead Baseline quarterly; and (ii) will adjust the BVT Overhead Baseline at the beginning of each of the Second Five Year Efficiency Savings

Period and Third Five Year Efficiency Savings Periods (in the case of (ii) only in accordance with Clause 18.6),

in each case, where the MoD and BVT (acting through the JPO) agree that the BVT Overhead Baseline may be adjusted to take into account the following factors:

- (a) Actual Workload;
- (b) changes to BVT's projected workload as set out in BVT's 10 Year Business Plan;
- (c) any final agreement between the MoD and BAES on pensions; and
- (d) other agreed adjustments (such as one-off costs) to the BVT Cost Base from time to time,

(the **Key Assumptions**).

Recommendations after review

- 14.1.7 If the JPO review finds that there have been changes in the Key Assumptions, the JPO shall recommend to the Steering Group that the BVT Overhead Baseline is adjusted in accordance with Clause 14.1.6. The BEM shall be used as a tool to inform discussions between the MoD, BVT and CAAS in relation to the adjustment of the BVT Overhead Baseline but shall not be conclusive.
- 14.1.8 If the Steering Group has endorsed an adjustment to the BVT Overhead Baseline (and if CAAS) has audited such adjustment) the BVT Overhead Baseline shall be amended accordingly (and the BEM shall be revised to reflect such adjustment) and such adjusted BVT Overhead Baseline shall become the BVT Overhead Baseline for the purposes of this Contract for the remainder of the Contract Period.

Baseline for Other Savings

- 14.1.9 The Baseline with respect to other Delivered Efficiency Savings (other than in relation to the BVT Overhead Baseline) (**Other Savings**) will be measured and agreed on a case by case basis. The principles for the methodology against which the Baseline for Other Savings will be calculated are as follows:
 - (a) auditable by CAAS;
 - (b) agreed by both the MoD and BVT;
 - (c) capable of being a fair reflection of Efficiency Savings actually made;
 - (d) trackable in accordance with Clause 16 (*Benefit Tracking and Realisation Process*);
 - (e) for direct labour, a complete direct labour baseline shall include the following elements: labour rate, productive hours and output (including a timeline) measures
 - (f) for direct materials, a complete direct materials baseline will include material costs, material volume, output and waste measures; and
 - (g) other principles to be agreed from time to time by the MoD and BVT (acting through the JPO).

Without prejudice to these principles, BVT and the MoD acknowledge that any Baseline may include defined and robust assumptions.

14.1.10 It is acknowledged by the MoD and BVT that for the purposes of calculating Delivered Efficiency Savings, where possible reference will be made to operational metrics as at 1 January 2007.

14.2 Miscellaneous

Adjustment of Trend Rates

14.2.1 Immediately a Transformation Benefit Proposal becomes an Approved Transformation Benefit Proposal, the MoD shall take into account Efficiency Savings when setting the Trend Rates.

BAES HQ charges

14.2.2 BVT and the MoD acknowledge that the actual HQ charge for BVT (the HQ Charge) shall continue to be agreed annually between the appropriate MoD authority and BAES head office.

14.2.3 The MoD and BVT agree that, if the HQ Charge increases above the amount allocated to it within the BVT Overhead Baseline for 2008/2009, the BVT Overhead Baseline for 2008/2009 shall not be amended to reflect such increase.

14.2.4 Notwithstanding this Clause 14.2, BVT's obligation to achieve the Guaranteed Minimum Target shall remain. However, BVT and the MoD shall agree appropriate adjustment to the relevant Cumulative Guaranteed Minimum Savings Yearly Targets to take into account any increase in the HQ charge to the extent that it varies above the amount contained within the BVT Overhead Baseline for 2008/2009.

14.2.5 Following the sale by VTG of its shareholding in BVT pursuant to Clause 48 (*VTG Exit*), BAES shall use its reasonable endeavours to ensure that the HQ Charge paid to it by BVT are set at an appropriate level to reflect the volume of work going through the business, subject always to any relevant indexation.

14.3 Cumulative Guaranteed Minimum Savings Yearly Targets and Termination

14.3.1 Until such time as BVT has delivered £350 million (three hundred and fifty million pounds) (Indexed) in aggregate of Delivered Efficiency Savings, the failure by BVT to achieve during any period of 2 consecutive years the Cumulative Guaranteed Minimum Savings Yearly Target as set out in Part 3 of Schedule 5 (*Integration, Transformation and Strategic Rationalisation*) shall be a BVT Default which shall entitle MoD to terminate this Contract. The MoD acknowledges that the Banked Efficiency Savings shall count towards the achievement of the first Cumulative Guaranteed Minimum Savings Yearly Target.

14.3.2 Without prejudice to Clause 18.4 the recurring benefit of Delivered Efficiency Savings, shall be counted for the entirety of the Initial Term (rather than for a maximum of five years) when assessing whether the Cumulative Guaranteed Minimum Savings Yearly Targets have been met by BVT.

15 Performance Review

15.1 General

The performance of BVT under this Contract will be monitored by the JPO. The JPO will provide reports to the Steering Group on a quarterly and annual basis as described below in Clause 15.3 (*JPO Reporting Obligations*).

Part 7 – Key Industrial Capability

20 Key Industrial Capability

20.1 Underlying obligation

20.1.1 Subject to the MoD complying with its material obligations under this Part 7 (*Key Industrial Capability*), BVT undertakes from the date of this Contract to contribute to the sustainment of Sovereign Capability and to satisfy the Surface Ship Capability through the provision and maintenance of the Key Industrial Capability.

Surface Ship Capability

20.1.2 The Surface Ship Capability is the ability for BVT to:

- (a) design, build and integrate (including complex systems integration) a complex warship of up to 5,000 tonnes deep displacement at an interval of 1 shipbuild every 12 months and a design interval of every 6 years; and
- (b) support the MoD naval vessels to meet operational requirements and in this regard BVT must be capable of:
 - (i) class output management and related technical services;
 - (ii) performing defect repair and maintenance tasks;
 - (iii) fitting urgent operational requirement (**UOR**) capability enhancements;
 - (iv) survey and deep maintenance tasks;
 - (v) providing maritime system defects diagnosis;
 - (vi) commissioning and testing;
 - (vii) meeting surge demands;
 - (viii) fleet-time and upkeep engineering;
 - (ix) maintenance of naval and dockyard facilities.

Acknowledgement regarding Key Posts

20.1.3 It is acknowledged by the MoD and BVT that Assumed Man-hours Capability for each Key Post set out in Part 1 and Part 2 of Schedule 4 (*Key Industrial Capabilities*) have been jointly formulated, and these numbers are an estimate of the minimum core personnel and skilled labour but do not reflect the actual size of the workforce which may, as envisaged at the date of this Contract, be needed to meet the Surface Ship Capability. In addition the Assumed Man-hours Capability is not linked to or based on any particular Assumed Workload for BVT for either shipbuild or support during the Contract Period.

Key Worker location and employment

20.1.4 All Key Post Workers must be:

- (a) located in the United Kingdom; and
- (b) employed by BVT or a BVT Subsidiary or by an Approved Sub-Contractor.

20.2 The Shipbuilding KIC

Shipbuilding - Key Posts

BVT will be deemed to satisfy the Surface Ship Capability in relation to the Shipbuilding KIC by maintaining the Assumed Man-hours Capability for each Key Post in the following sectors for shipbuilding (the **Shipbuilding Sector**):

- (a) production;
- (b) direct support staff; and
- (c) design/engineering.

21 The Support KIC

General

- 21.1 The MoD and BVT agree and acknowledge that the sustainment and need to satisfy the Surface Ship Capability and Sovereign Capability extend to the provision of Maintenance.

Support - Key Posts

- 21.2 BVT will be deemed to satisfy the Surface Ship Capability in relation to the Support KIC by maintaining the Assumed Man-hours Capability for each Key Post in the following sectors for support (the **Support Sector**):

- (a) initial support;
- (b) blue collar engineering;
- (c) white collar engineering;
- (d) supply chain and warehousing; and
- (e) facilities and warehousing.

Acknowledgement

- 21.3 It is acknowledged that the Support KIC will be subject to further in-depth review at the Strategic Review in 2011 which may result in a KIC Adjustment in relation to the Support Sector provided that the Support KIC Cap and Support KIC shall not be varied unless both BVT and the MoD agree otherwise pursuant to a Change in accordance with Clause 51 (*Change Procedure*).

22 Facilities

BVT obligation

- 22.1 BVT shall maintain its own Facility, or have unfettered access to a Facility owned and operated by an Approved Sub-Contractor, in both cases within the United Kingdom which are maintained sufficiently to enable it to satisfy the Surface Ship Capability and which comply with Legislation.

Acknowledgement regarding overheads for shipbuilding

- 22.2 The Shipbuilding Overhead KIC Cap has been agreed between BVT and the MoD on the basis that, in order to satisfy the Surface Ship Capability, in relation to shipbuilding BVT is

required to maintain a single Shipbuilding Facility (or equivalent) in the United Kingdom. In the event that BVT continues to operate or have access to more than one Shipbuilding Facility (or equivalent) in the United Kingdom, and a KIC Overhead Trigger Event has occurred, then any additional overhead charges in excess of the Shipbuilding Overhead KIC Cap shall solely be for the account of BVT.

Facilities

- 22.3 BVT shall not surrender and BVT shall procure that no BVT Subsidiary shall surrender the lease to any Facility which is from time to time necessary for it to discharge its obligation in Clause 22.1 without the prior written approval of the MoD (in the MoD's absolute discretion), unless and to the extent that such transaction is in favour of an Approved Sub-Contractor.

23 KIC Trigger Events and KIC Payments

KIC Notice

- 23.1 BVT shall notify the MoD in writing (a **KIC Notice**) as soon as reasonably practicable where a Monthly Sales and Operational Plan Review identifies that there is a prospective Workload Shortfall in the following 3 Months and the occurrence of a KIC Trigger Event is likely. BVT shall submit copies of the relevant Monthly Sales and Operational Plan Review to the MoD, provided, however, that BVT may satisfy its obligation to submit copies of such reports by doing so through the JPO.

Mitigation of MoD's liability before notice

- 23.2 BVT shall at all times prior to serving a KIC Notice proactively take all reasonable steps to minimise, mitigate and/or reduce the MoD's liability to make KIC Payments.

Mitigation after receipt of KIC notice

- 23.3 Following receipt of the KIC Notice, BVT and the MoD shall consult as soon as reasonably practicable in accordance with Clause 29 (*Partnering*) and the Partnering Principles to identify mitigation measures against the occurrence of the Workload Shortfall. BVT shall proactively take all reasonable steps to minimise, mitigate and/or reduce the MoD's liability to make KIC Payments by pursuing the following options:
- 23.3.1 BVT pursuing export opportunities or any other related opportunities to utilise Key Post Workers provided that any contracts with third parties are competed and won on an arm's-length and "full-cost" basis (with no cross subsidy from the MoD) and, where any BVT Group Company is awarded any export or related shipbuilding contracts and there is a Workload Shortfall at such time, BVT shall use all reasonable endeavours, subject to any local sourcing restrictions, to utilise any Available Key Workers to work on such contracts to the extent that there is a requirement for the Relevant Trade;
 - 23.3.2 without prejudice to Clause 9 (*Exclusivity*), the possibility of the MoD bringing forward contracts for construction of Naval Vessels and/or Work provided it is acknowledged that the MoD is not required under this Contract at any time to procure or order any Naval Vessels or Work from BVT;
 - 23.3.3 following the Strategic Review in 2011, if agreed (and provided it does not conflict with any existing contractual arrangements) between BVT and the MoD, a Through Life Capability Management option for Naval Vessels;
 - 23.3.4 BVT and the MoD liaising with members of SSSA or any other relevant entity to second employees (on terms to be agreed) to a relevant entity to assist with MoD-related or other contracts provided that, where a Key Post Worker is utilised by a third party, BVT shall be entitled to retain any profit element agreed with such third party associated with the use of such a Key Post Worker;

Part 8 – Partnering

29 Partnering

Partnering obligation

29.1 In seeking to achieve the Commercial Purpose in accordance with Clause 7 (*Commercial Purpose*) (without limitation), the MoD and BVT shall each:

- (a) comply with Clause 29.2; and
- (b) seek to act at all times in accordance with the Partnering Principles.

Specific partnering obligations

29.2 The MoD and BVT shall each additionally:

- (a) collaborate with the other to the maximum extent possible;
- (b) establish within its organisation internal arrangements, including as to the deployment, leadership, training and development of personnel, sufficient at all times to ensure that:
 - (i) the relationship contemplated by this Contract functions fully and efficiently in the manner best calculated to achieve the Commercial Purpose; and
 - (ii) all its personnel engaged in relation to the management of the relationship between the MoD and BVT understand and act in accordance with this Contract, in particular the requirements of this Clause 29 (*Partnering*);
- (c) establish within 3 months of the Commencement Date a Relationship Management Plan and thereafter implement, continuously monitor and improve over time the effectiveness of the Relationship Management Plan;
- (d) continuously seek to improve the efficiency of the relationship between them, which shall be measured using an appropriate relationship management tool to be agreed and adopted by the JPO; and
- (e) in particular, cooperate to demonstrate how, and the extent to which, each and all aspects of the relationship between the MoD and BVT, and each Project Contract between them, delivers value for money to the MoD.

Strategic Partnering Accord

29.3 Schedule 7 (*Partnering*) sets out the Strategic Partnering Accord between the MoD and BVT.

29.4 The Strategic Partnering Accord:

- (a) contains at section 5 (*the Partnering Principles*) in relation to which Clause 29.1(b) of this Contract applies;
- (b) is intended to be a working level summary of some of the rights and obligations in this Contract, produced for the purpose of informing the personnel of the MoD and BVT about how this Contract obliges the MoD and BVT to work together to deliver the Commercial Purpose;
- (c) as such, is not itself legally binding (though Clause 29.1(b) of this Contract is), does not amend, limit or override this Contract and shall at all times be read and construed

as subject to this Contract, and in the case of any inconsistency, shall be amended to be consistent with this Contract;

- (d) shall not be admissible as evidence of the intentions of the MoD and BVT when entering into this Contract;
- (e) may not be amended unless to the extent that:
 - (i) it remains consistent in its entirety with this Contract; and
 - (ii) all amendments are approved by the JPO; and
- (f) shall not be capable of being produced as evidence that the MoD or BVT has waived or accepted performance which is inconsistent with this Contract.

29.5 Neither the MoD nor BVT may rely on the terms of the Strategic Partnering Accord to excuse non-compliance with this Contract and compliance with the Strategic Partnering Accord shall not reduce or limit any obligation of the MoD or BVT under this Contract nor permit altered or reduced performance or non-performance thereof.

30.6 The Supply Chain Principles

BVT shall use all reasonable endeavours to comply with the following principles when implementing the Overarching Supply Chain Strategy, the Project Supply Chain Strategies and the Category Supply Chain Strategies and managing its supply chain:

- (a) to strive for the highest professional standards in the award of contracts, usually by means of competition, so as to maximise efficiency;
- (b) to make available sufficient time and information for suppliers to respond to the bidding process appropriate for the work, and to define and publicise amongst the supplier community contact points for the handling of enquiries and complaints;
- (c) to preserve genuine competition and avoid discrimination;
- (d) to provide opportunities on an even-handed basis for suppliers (whether BVT itself, BVT Subsidiaries or external suppliers) to participate in competitions, but, in the interests of both customer and suppliers, limiting numbers to ensure optimum economy, whilst honouring (and testing, where appropriate) preferred supplier status and strategic alliances;
- (e) to make available to the MoD the criteria for the evaluation of bids, to evaluate bids objectively and to notify the outcome promptly to competing suppliers and to avoid improper business practices;
- (f) to use sensible risk-sharing arrangements whilst using incentivisation techniques to encourage innovation and improve performance;
- (g) to consult with the MoD and, where applicable, use the Government Profit Formula and any applicable costing and pricing conventions when agreeing prices for non-competitive sub-contracts;
- (h) to strive for the highest professional standards in the management of contracts;
- (i) to pay promptly for work done in accordance with the relevant contractual terms;
- (j) to assess supplier performance in an objective and open manner and apply those assessments coherently in the process of supplier selection and tender evaluation; and
- (k) to comply with relevant good procurement process.

30.7 Competitive Procurement

30.7.1 It is acknowledged by BVT that the MoD favours competition as the preferred means of supplier selection for its defence requirements and it wishes to see the greatest application of competition by BVT for supply chain activities. Accordingly BVT shall use all reasonable endeavours to carry out and be responsible for the placing of Sub-Contracts on a competitive basis with such contracts awarded to tenderers who comply with the tender requirements except where otherwise identified in Clause 30.8 (*Sole Source or BVT Supply*). It is acknowledged, however, by the MoD that BVT may also secure demonstrable value for money for both MoD and BVT from the supply chain by establishing longer-term strategic relationships with suppliers.

30.7.2 BVT shall ensure that prior to the award of any Sub-Contract for a Works Item to be procured on a competitive basis in excess of the Threshold Level it shall:

- (a) invite the MoD to comment on, and provide input for, proposed tender requirements, selection criteria and tender evaluation requirements;