

VIA EMAIL

IN CONFIDENCE

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Tuesday 24th January 2012

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Dear Ben,

RE: 2012 MPG and equivalent grades Pay Review.

I am writing following our meeting on Monday 22nd January and I am pleased to set out Telefonica UK's final offer in respect of this year's pay review and covering a two year period to 1st March 2014. This offer is conditional on the understanding that Prospect will recommend this settlement to members. I understand that any ballot will be conducted through the usual e-ballot of members which would commence on Monday 30th January, closing on Monday 6th February.

The offer is a two year offer with a budget for pay increases in 2012 of 2.75% and a budget for increases in 2013 of 2.5%. Distribution methodology will be as follows. For all roles other than those in retail we are proposing a distribution matrix for 2012 that takes account of position against the market and APR score as outlined in the grid below. The indicative market pay benchmark points for each job family are detailed in the appendix attached.

The percentage pay increase ranges for these roles are as follows:

| | APR 1 | APR 2 | APR 3 | APR 4 |
|-------------------------------|------------|----------|-------------|-------|
| Upper Quartile against market | 0 – 2.5 | 0 – 1.5 | 0 – 1 | 0 |
| Upper Middle Quartile | 2.25 – 3.5 | 2 – 2.75 | 1.75 – 2.5 | 0 |
| Lower Middle Quartile | 2.75 – 4.5 | 2.5 – 4 | 2.25 – 3.25 | 0 |
| Lower Quartile | 3.5 – 5.5 | 3 – 4.5 | 2.75 – 3.75 | 0 |

In Retail, because of the salary distribution of these roles we have had to design a slightly different distribution matrix to ensure that the budget can be delivered. The budget available in retail will still be 2.75%.

Retail Distribution Matrix:

| | APR 1 | APR 2 | APR 3 | APR 4 |
|--------------------------------------|--------------|--------------|--------------|--------------|
| Upper Quartile against market | 0 – 2.5 | 0 – 1.5 | 0 – 1 | 0 |
| Upper Middle Quartile | 2.25 – 3.5 | 1.75 – 2.75 | 1.5 – 2.5 | 0 |
| Lower Middle Quartile | 2.75 – 4.5 | 2.5 – 4 | 2 – 3 | 0 |
| Lower Quartile | 3.5 – 5.5 | 3 – 4.5 | 2.5 – 3.5 | 0 |

Managers will be instructed that the minimum levels of ranges indicated must be awarded to employees with the only exception being, where to do so, would exceed the agreed budget. Awards above the minimum will be at management discretion.

Additionally having reviewed the relevant pay ranges against the wider market we propose to make the following changes to the pay range maximum and minimums for 2012.

MPG2 minimum to increase from £22,500 to £23,000 and maximum to increase from £39,600 to £40,000

MPG4 minimum to increase from £26,000 to £29,000

PSG1 minimum to increase from £20,000 to £21,000

PSG2 minimum to increase from £25,000 to £25,750

RCGS1/10 minimum to increase from £16,000 to £16,200

RCGS2/20 minimum to increase from £22,000 to £22,500 and maximum to increase from £27,500 to £28,000

We can also confirm that following the completion of our joint review which we undertook as part of the 2010 pay review settlement, the company agree to allocate a budget of £155,000 (equivalent to 0.25% of overall pay bill) to resolve the identified issues of Manager differentials and comparative anomalies identified through the joint review. It would be our intention to distribute this budget by identifying those employees who currently do not enjoy a reasonable minimum differential in comparison with those employees they manage and allocate the necessary proportion of the budget to address this issue. Our priorities will be those whose total reward is less than 10% greater than those they manage with particular emphasis on basic pay elements of total reward.

Subject to the timely and satisfactory conclusion of your membership ballot, increases will be effective from 1st March 2012 and will be included in March salaries. As is always the case following implementation of the pay deal we would meet with you to share the relevant outcomes.

Yours sincerely

Martin Lally
Head of Employee Relations

Attachment Indicative market pay benchmark points for each job family



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Head of Employee Relations
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26 January 2012

By email

Dear Martin

2012 MPG and equivalent grades Pay Review

Thank you for your letter of 24 January 2012 setting out Telefónica UK's final offer for the 2012/2013 pay reviews. I can confirm that the union's negotiators will be recommending this offer to members in the e-ballot that will open at 4pm on Monday 30 January and close at 4pm on Monday 6 February.

As you know, we do have some concerns with this offer. Although the budget on offer is broadly in line with the generality of settlements currently being made in the private sector of the UK economy, there are a number of aspects to the proposed agreement that do give cause for concern and I said that I would write to you setting these out.

However, before doing so we do need to place on record our appreciation of the fact that the offer does include a far greater degree of transparency than has been available before. The combination of the matrix and the publication of the pay ranges for every job family to which our members are mapped does mean that for the first time, members will be able to see what the minimum increase for them should be (although you have been careful to point out that whilst the minimum increase in each box should be achievable you cannot be absolutely certain of that – and where there is exceptionally insufficient budget, then this may not be achievable).

We view this as an extremely important and welcome development in the company's approach to reward. It means that, in future, we will be able to look at market data and hopefully negotiate on, and agree, pay ranges for each of these job families (or roles) and get away from the outmoded and increasingly meaningless MPG2 and MPG 4 pay ranges, which now serve largely only to confuse our members and render the reward policies of the company somewhat opaque.

~~Our concerns with this offer are, however:~~

- The pay rate for the Customer Service Operations role at MPG 2 is in our view significantly too low. The company proposes a median pay rate for jobs in this family of just £24,500, based on external market data. The company's own pay data shows that the median rate actually paid by TUK is around £27,000 (across this job family as a whole) and we know from our agreements with other companies in the IT and telecoms space that a more appropriate rate would be closer to £28,000-£29,000. Most of our members in this job family are likely to see no or very small increases from this proposed settlement, which inevitably means that securing member support for the offer won't be easy.
- The legacy of the past several years of pay settlements in O2 does tend to mean that a significant number of our members are paid at rates that bear little relationship to the market rates set out in the annex to your letter. For example we have recently conducted a survey of our members in the Radio Access Network area and this has disclosed that individuals can be paid as little as £26,000 and as much as £50,000 a year for the same or a very similar job (certainly these are jobs falling within the same family) and where there is no obvious reasons for these wide disparities. Inevitably therefore there is a legacy that the new and more transparent approach can only erode over time and this too will present us with a significant issue in seeking to secure member support for this offer
- Ideally we would have wanted to examine and seek to agree the appropriateness of the pay ranges for each of the job families. This has not been feasible for this proposed settlement as there simply has not been time. In future years we would need to make time for this process. I should add that the union is comfortable with a market data-led approach to the setting of pay rates, as such an approach is fair to our members and to the company itself and its stakeholders, and should result in the company paying its employees both fairly and competitively in relation to the market. But experience shows that there is a need for a dialogue about the data and how the firm interprets it and seeks to reflect it into its own reward policies.
- Whilst the overall budget is broadly in keeping with the generality of settlements, we do remain concerned that this budget is likely to be stretched to the limit – and possibly beyond, in the sense that it is unlikely to be sufficient in the longer term to provide both fair increases to reflect the rising cost of living and a fair measure of pay progression to those paid significantly below the appropriate market rate for their job family. Over time we will have to address this – and the greater transparency afforded by the approach to pay will increase the pressure on both the company and the union to address this concern around pay progression.

In summary, the union's negotiators will be recommending this offer but we cannot be sanguine about the outcome of the e-ballot and it is also clear to us that this agreement, should we make it, would represent the first positive step on a journey.

Yours sincerely

Ben Marshall
Assistant General Secretary

INDICATIVE MARKET RANGES PER JOB FAMILY PER GRADE

TOTAL TARGET CASH LEVELS SHOWN FOR SALES AND RETAIL ROLES

The information shown are averages from two or more market data sources.

| | | BASE SALARY | | | | |
|--|--|------------------|--------------------|--------------------|-------------------|---------|
| | | <=Lower quartile | Lower Mid quartile | Upper Mid quartile | >= Upper quartile | |
| | | Up to 25th % | 25%-50% | 50%-75% | 75% or above | |
| MPG2 | Finance | £27,125 | £27,126 - £30,106 | £30,107 - £33,116 | £33,117 | |
| | Marketing | £26,797 | £26,798 - £28,957 | £28,958 - £32,340 | £32,341 | |
| | Customer Services Operations | £23,000 | £23,001 - £24,500 | £24,501 - £27,000 | £27,001 | |
| | Administrative Services | £30,767 | £30,768 - £32,566 | £32,567 - £36,282 | £36,283 | |
| | Project Management | £27,761 | £27,762 - £30,079 | £30,080 - £32,954 | £32,955 | |
| | IT Development | £29,941 | £29,942 - £32,687 | £32,688 - £36,807 | £36,808 | |
| | Technology Product Support / Development | £30,100 | £30,101 - £35,777 | £35,778 - £39,523 | £39,524 | |
| | Technical Services & Support | £24,817 | £24,818 - £26,717 | £26,718 - £32,012 | £32,013 | |
| | Technical Speciality | £30,074 | £30,075 - £33,567 | £33,568 - £33,036 | £36,037 | |
| | Engineering | £30,759 | £30,760 - £33,304 | £33,305 - £36,952 | £36,953 | |
| | Human Resources | £25,106 | £25,107 - £27,724 | £27,724 - £30,973 | £30,974 | |
| | MPG4 | Finance | £35,189 | £35,190 - £38,197 | £38,198 - £41,563 | £41,564 |
| | | Marketing | £33,174 | £33,175 - £39,049 | £39,050 - £42,243 | £42,244 |
| Customer Services Operations | | £33,200 | £33,201 - £36,599 | £36,600 - £42,300 | £42,301 | |
| Supply Chain Management | | £35,155 | £35,156 - £37,593 | £37,594 - £39,181 | £39,182 | |
| Corporate Affairs / Comms | | £33,406 | £33,407 - £35,853 | £35,854 - £39,139 | £39,140 | |
| Project Management | | £34,740 | £34,741 - £37,828 | £37,829 - £41,914 | £41,915 | |
| IT Development | | £36,394 | £36,395 - £38,464 | £38,465 - £42,182 | £42,183 | |
| Technology Product Support / Development | | £39,449 | £39,450 - £43,654 | £43,655 - £47,340 | £47,341 | |
| Technical Services & Support | | £38,723 | £38,724 - £41,524 | £41,525 - £45,000 | £45,001 | |
| Technical Speciality | | £37,550 | £37,551 - £41,932 | £41,933 - £46,266 | £46,267 | |
| Engineering | | £40,644 | £40,645 - £43,354 | £43,355 - £46,867 | £46,868 | |
| Human Resources | | £33,888 | £33,889 - £37,912 | £37,913 - £45,369 | £45,370 | |

| | | <=Lower quartile | Lower Mid quartile | Upper Mid quartile | >= Upper quartile |
|-----------|-------------------------|------------------|--------------------|--------------------|-------------------|
| | | Up to 25th % | 25%-50% | 50%-75% | 75% or above |
| | | PSG1 | Account Management | £22,500 | £22,501 - £24,146 |
| Telesales | £21,653 | | £21,654 - £22,304 | £22,304 - £23,432 | £23,433 |
| PSG2 | Account Management | £30,482 | £30,483 - £33,559 | £33,560 - £36,504 | £36,505 |
| | Relationship Management | £30,178 | £30,179 - £32,499 | £32,500 - £35,669 | £35,670 |
| | Channel Sales | £30,330 | £30,331 - £33,208 | £33,209 - £36,087 | £36,088 |

| TOTAL TARGET CASH (BASE SALARY + TARGET BONUS) | | | |
|--|--------------------|--------------------|-------------------|
| <=Lower quartile | Lower Mid quartile | Upper Mid quartile | >= Upper quartile |
| £25,875 | £25,876 - £27,728 | £27,729 - £29,582 | £29,583 |
| £24,901 | £24,901 - £25,923 | £25,924 - £26,947 | £26,948 |
| £38,103 | £38,104 - £41,866 | £41,867 - £45,630 | £45,631 |
| £37,723 | £37,724 - £41,154 | £41,155 - £44,587 | £44,588 |
| £37,913 | £37,914 - £41,510 | £41,511 - £45,108 | £45,109 |

| | | <=Lower quartile | Lower Mid quartile | Upper Mid quartile | >= Upper quartile |
|---|---------|------------------|------------------------------------|--------------------|-------------------|
| | | Up to 25th % | 25%-50% | 50%-75% | 75% or above |
| | | Retail | Store Leader (Category 1) - RCGS30 | £25,999 | £26,000 - £26,999 |
| Store Leader (Category 2) - RCGS20 | £23,875 | | £23,876 - £25,249 | £25,250 - £26,624 | £26,625 |
| Store Leader (Category 3) - RCGS10 | £20,749 | | £20,750 - £21,499 | £21,500 - £22,249 | £22,250 |
| Asst Store Leader (Category 1) - RCGS10 | £17,750 | | £17,751 - £18,499 | £18,500 - £19,249 | £19,250 |
| Asst Store Leader (Category 2) - RCGS10 | £16,650 | | £16,651 - £17,099 | £17,100 - £17,549 | £17,550 |
| Guru (RCGS10) | £17,900 | | £17,901 - £19,599 | £19,600 - £21,299 | £21,300 |

| TOTAL TARGET CASH (BASE SALARY + TARGET BONUS) | | | |
|--|--------------------|--------------------|-------------------|
| <=Lower quartile | Lower Mid quartile | Upper Mid quartile | >= Upper quartile |
| £32,499 | £32,500 - £33,751 | £33,750 - £34,999 | £35,000 |
| £29,844 | £29,845 - £33,280 | £31,563 - £33,281 | £33,281 |
| £24,484 | £24,485 - £25,369 | £25,370 - £26,254 | £26,255 |
| £20,945 | £20,946 - £21,829 | £21,830 - £22,714 | £22,715 |
| £19,647 | £19,648 - £20,177 | £20,178 - £20,708 | £20,709 |
| £20,585 | £20,585 - £22,539 | £22,540 - £24,494 | £24,495 |

