

IUS CONSOLIDATED CONTRACT SCHEDULE

CONSOLIDATED SCHEDULE 12

EXCESS PROFIT SHARING

for Contract Number DCNS/119

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CONSOLIDATED SCHEDULE 12

EXCESS PROFIT SHARING

This Consolidated Schedule sets out the Customer Authority's special terms relating to excess profit sharing.

Capitalised terms used but not defined in this Consolidated Schedule are defined in Consolidated Schedule 1 (*Definitions*).

1 INTRODUCTION

- 1.1** This Consolidated Schedule details the method by which the Customer Authority will share in any Profits made by the Contractor in connection with the provision of the Services, where such Profits are above the Target Profit Margin. The Customer Authority's share of any Profits above the Target Profit Margin is set out in Appendix 1 to this Consolidated Schedule.
- 1.2** In particular, this Consolidated Schedule sets out provisions relating to:
- 1.2.1** the Excess Profit Share and how it relates to the Profit (see Paragraph 2 below);
 - 1.2.2** the calculation of the Excess Profit Share (see Paragraph 3 below);
 - 1.2.3** the application of the Excess Profit Share Calculations (see Paragraph 4 below); and
 - 1.2.4** disputes regarding the Excess Profit Share (see Paragraph 5 below).

2 EXCESS PROFIT SHARE

- 2.1** All Profit above the Target Profit Margin shall be shared between the Contractor and the Customer Authority in accordance with the provisions of this Consolidated Schedule and the Excess Profit Sharing Table as set out in Appendix 1 to this Consolidated Schedule.

3 EXCESS PROFIT SHARE CALCULATION

- 3.1** The Contractor shall deliver to the Customer Authority the Excess Profit Share Calculations:
- 3.1.1** in accordance with Consolidated Schedule 10 (*Financial Model*);
 - (i) as a standalone document to be delivered in accordance with this Paragraph 3.1; and
 - (ii) as part of each of the Financial Model including each Contract Annual Account;
 - 3.1.2** within thirty (30) Working Days after the earlier of:
 - (i) the date on which the Initial Term ends; and
 - (ii) the date upon which this Consolidated Contract terminates following either Party exercising its right to terminate this Consolidated Contract in accordance with Clause 47 (*Termination Rights*) of this Consolidated Contract,

for the Relevant Profit Period commencing on the Contract Date and ending on the date referred to in 3.1.2(i) or 3.1.2(ii) (as applicable);

3.1.3 (if applicable) within thirty (30) Working Days after the earlier of:

- (i) the date on which the first Extension Period (if any) ends; and
- (ii) the date upon which this Consolidated Contract terminates during the first Extension Period following either Party exercising its right to terminate this Consolidated Contract in accordance with Clause 47 (*Termination Rights*) of this Consolidated Contract,

for the Relevant Profit Period commencing on the first day of the first Extension Period and ending on the date referred to in 3.1.3(i) or 3.1.2(ii) (as applicable); and

3.1.4 (if applicable) within thirty (30) Working Days after the earlier of:

- (i) the date on which the second Extension Period (if any) ends; and
- (ii) the date upon which this Consolidated Contract terminates during the second Extension Period following either Party exercising its right to terminate this Consolidated Contract in accordance with Clause 47 (*Termination Rights*) of this Consolidated Contract,

for the Relevant Profit Period commencing on the first day of the second Extension Period and ending on the date referred to in 3.1.4(i) or 3.1.4(ii) (as applicable).

3.2 The Contractor shall ensure that each Excess Profit Share Calculation delivered to the Customer Authority in accordance with Paragraphs 3.1.2, 3.1.3 and 3.1.4 above in respect of each applicable Relevant Profit Period is certified by an External Auditor and a director of the Contractor as being accurate and not misleading.

3.3 For any given Relevant Profit Period, each Excess Profit Share Calculation shall include the calculations below:

3.3.1 Calculation of the percentage amount by which the Actual Profit Margin exceeds the Target Profit Margin

$$\text{Percentage Excess} = (\text{Actual Profit Margin} - \text{Target Profit Margin})$$

3.3.2 Calculation of Excess Profit

$$\text{Excess Profit} = \text{Percentage Excess} \times \text{Revenue}$$

3.3.3 Calculation of Excess Profit Share

Each Band, b , (as set out in Appendix 1 to this Consolidated Schedule) shall be an applicable Band for the purposes of determining the Excess Profit Share, where the following is satisfied:

$$\text{Lower Excess Profit Range } b < \text{Percentage Excess}$$

Each portion of Percentage Excess that falls within an applicable Band shall attract the Excess Profit Share relevant to that Band and shall be calculated as follows:

(i) **Calculation of Excess Profit Amount**

(a) For any applicable Band, where

$$\text{Percentage Excess} \geq \text{Upper Excess Profit Range}$$

an individual Excess Profit Share calculation shall be calculated as follows:

$$(Excess\ Profit / Percentage\ Excess) \times (Upper\ Excess\ Profit\ Range - Lower\ Excess\ Profit\ Range) \times Excess\ Profit\ Share$$

- (b) For any applicable Band, where

$$Lower\ Excess\ Profit\ Range \leq Percentage\ Excess < Upper\ Excess\ Profit\ Range$$

an individual Excess Profit Share calculation shall be calculated as follows:

$$(Excess\ Profit / Percentage\ Excess) \times (Percentage\ Excess - Lower\ Excess\ Profit\ Range) \times Excess\ Profit\ Share$$

(ii) **Calculation of Total Excess Profit Amount**

The “**Total Excess Profit Amount**” shall be the sum of the Excess Profit Amounts calculated as per Paragraph 3.3.3(i) above.

- 3.4** If any of the Excess Profit Share Calculations provided pursuant to Paragraphs 3.1.2, 3.1.3 and 3.1.4 above show that, in relation to the Relevant Profit Period, the Actual Profit Margin achieved by the Contractor is below or equal to the Target Profit Margin, then all of the Profit for such Relevant Profit Period shall be retained by the Contractor.
- 3.5** Without prejudice to Clause 22 (*Audits, Notifications and Record Keeping*) of this Consolidated Contract, the Contractor shall provide to the Customer Authority all information reasonably requested by the Customer Authority from time to time for the purpose of verifying the accuracy of the Excess Profit Share Calculations.

4 APPLICATION OF TOTAL EXCESS PROFIT SHARE CALCULATIONS

- 4.1** If any of the Excess Profit Share Calculations provided pursuant to Paragraphs 3.1.2, 3.1.3 and 3.1.4 above show that there is a Total Excess Profit Amount that is greater than zero, then the Contractor shall, at the Customer Authority’s request:
- 4.1.1** deduct any such Total Excess Profit Amount from the next invoice(s) due under this Consolidated Contract;
 - 4.1.2** pay directly to the Customer Authority any such Total Excess Profit Amount as a debt (subject to the operation of Paragraph 5 below) within ten (10) Working Days of the Customer Authority’s request; or
 - 4.1.3** provide to the Customer Authority a credit note to the value of any such Total Excess Profit Amount for use by the Customer Authority against future invoices at its discretion, within ten (10) Working Days of the Customer Authority’s request.

5 DISPUTES

- 5.1** The Customer Authority may inform the Contractor by written notice whether it disputes any item contained in any of the Excess Profit Share Calculations (an “**Excess Profit Share Notice**”). The Contractor shall within ten (10) Working Days of the date of such Excess Profit Share Notice either:

- 5.1.1** revise or clarify the relevant Excess Profit Share Calculation (or Excess Profit Share Calculations as the case may be) so as to address the Customer Authority's concerns, and deliver the same to the Customer Authority; or
 - 5.1.2** explain in writing to the Customer Authority that it does not agree with the position taken by the Customer Authority and provide the Customer Authority with such further financial information certified by the Contractor's External Auditors as is reasonably required by the Customer Authority to substantiate the Contractor's position to the Customer Authority's satisfaction.
- 5.2** Unless the Contractor responds to an Excess Profit Share Notice in accordance with Paragraph 5.1 above, then the Contractor shall pay to the Customer Authority as a debt an amount of two million five hundred thousand pounds sterling (£2,500,000), such sum to be retained by the Customer Authority until all of the Excess Profit Share Calculations are agreed by the Parties or determined by an Expert in accordance with the Dispute Resolution Procedure.

APPENDIX 1 **EXCESS PROFIT SHARING TABLE**

The table below shows the Excess Profit Share.

Band	Lower Excess Profit Range	Upper Excess Profit Range	Excess Profit Share
1	0.00%	1.00%	0.00%
2	1.00%	2.00%	15.00%
3	2.00%	3.00%	25.00%
4	3.00%	4.00%	40.00%
5	4.00%	5.00%	75.00%
6	5.00%	Actual Profit Margin (%)	100.00%

APPENDIX 2

WORKED EXAMPLE OF EXCESS PROFIT SHARE CALCULATIONS

In this example, the Relevant Profit Period is a five (5) year Initial Term and one (1) one (1) year Extension Period, over which the Services are provided. This Consolidated Contract is terminated after the first Extension Period. The Target Profit Margin is eight (8) per cent. for the Initial Term, and six (6) per cent. for the Extension Period, and the Revenue, Allowable Costs, Profit and Actual Profit Margin are as follows:

	Initial Term						Extension Period	
	Year 1	Year 2	Year 3	Year 4	Year 5	Total	Year 6	TOTAL
Revenue	£30,000	£38,000	£23,000	£21,000	£28,000	£140,000	£70,000	£70,000
Allowable Costs	£25,000	£33,200	£20,000	£20,000	£25,900	£123,900	£63,000	£63,000
Profit						£16,100		£7,000
Actual Profit Margin						11.5%		10%
Target Profit Margin						8%		6%

Calculation of Excess Profit for Initial Term

In accordance with Paragraph 3.1.2 above, the Excess Profit shall be calculated for the Relevant Profit Period starting at the Contract Date and ending on the date upon which the Initial Term ends.

Calculation of Actual Profit Margin

$$= \text{Profit} / \text{Revenue}$$

$$= £16,100 / £140,000$$

$$= 11.5\%$$

Calculation of Percentage Excess

$$= \text{Actual Profit Margin} - \text{Target Profit Margin}$$

$$= 11.5\% - 8\%$$

$$= 3.5\%$$

Calculation of Excess Profit

$$= \text{Percentage Excess} \times \text{Revenue}$$

$$= 3.5\% \times £140,000$$

$$= £4,900$$

Calculation of Excess Profit Share

In accordance with Paragraph 3.3.3 above, a Band, b , shall be an applicable Band for the purposes of determining the Excess Profit Share, where the following is satisfied:

$$\text{Lower Excess Profit Range } b < \text{Percentage Excess}$$

Band <i>b</i>	Lower Excess Profit Range	Upper Excess Profit Range	Is this an applicable Band (i.e. is the Lower Excess Profit Range lower than 3.5%)?
1	0.00%	1.00%	Yes
2	1.00%	2.00%	Yes
3	2.00%	3.00%	Yes
4	3.00%	4.00%	Yes
5	4.00%	5.00%	No
6	5.00%	Actual Profit Margin (%)	No

From the above, only Bands 1, 2, 3 and 4 are applicable Bands.

Calculation of Excess Profit Amounts

In accordance with 3.3.3(i)(a) above, the Excess Profit Amount for Bands 1, 2 and 3 shall be calculated as follows:

Band 1 Excess Profit Amount
 $(£4,900 / 3.5\%) \times (1\% - 0\%) \times 0\% = £0$

Band 2 Excess Profit Amount
 $(£4,900 / 3.5\%) \times (2\% - 1\%) \times 15\% = £210$

Band 3 Excess Profit Amount
 $(£4,900 / 3.5\%) \times (3\% - 2\%) \times 25\% = £350$

In accordance with 3.3.3(i)(b) above, the Excess Profit Amount for Band 4 shall be calculated as follows:

Band 4 Excess Profit Amount
 $(£4,900 / 3.5\%) \times (3.5\% - 3\%) \times 40\% = £280$

Calculation of Total Excess Profit Amount

In accordance with 3.3.3(ii), the Total Excess Profit Amount shall be the sum of all individual Excess Profit Amounts calculated for each applicable Band. Therefore, the Total Excess Profit Amount shall be calculated as follows:

Band 1 Excess Profit Amount + Band 2 Excess Profit Amount + Band 3 Excess Profit Amount + Band 4 Excess Profit Amount
 $= £210 + £350 + £280$
 $= £840$

Calculation of Excess Profit for Extension Period

In accordance with Paragraph 3.1.3 above, the Excess Profit shall be calculated for the Relevant Profit Period starting at the first day of the first Extension Period and ending on the date upon which the last Extension Period ends.

Calculation of Actual Profit Margin

= Profit / Revenue

= £7,000 / £70,000

= 10%

Calculation of Percentage Excess

= Actual Profit Margin – Target Profit Margin

= 10% - 6%

= 4%

Calculation of Excess Profit

= Percentage Excess x Revenue

= 4% x £70,000

= £2,800

Calculation of Excess Profit Share

In accordance with Paragraph 3.3.3 above, a Band, b , shall be an applicable Band for the purposes of determining the Excess Profit Share, where the following is satisfied:

Lower Excess Profit Range b < Percentage Excess

Band b	Lower Excess Profit Range	Upper Excess Profit Range	Is the Band Applicable?
1	0.00%	1.00%	Yes
2	1.00%	2.00%	Yes
3	2.00%	3.00%	Yes
4	3.00%	4.00%	Yes
5	4.00%	5.00%	No
6	5.00%	Actual Profit Margin (%)	No

From the above, only Bands 1, 2, 3 and 4 are applicable Bands

Calculation of Excess Profit Amount

In accordance with 3.3.3(i) above, the Excess Profit Amount for Bands 1, 2, 3 and 4 shall be calculated as follows:

Band 1 Excess Profit Amount

$$(\pounds 2,800 / 4\%) \times (1\% - 0\%) \times 0\% = \pounds 0$$

Band 2 Excess Profit Amount

$$(\pounds 2,800 / 4\%) \times (2\% - 1\%) \times 15\% = \pounds 105$$

Band 3 Excess Profit Amount

$$(\pounds 2,800 / 4\%) \times (3\% - 2\%) \times 25\% = \pounds 175$$

Band 4 Excess Profit Amount

$$(\pounds 2,800 / 4\%) \times (4\% - 3\%) \times 40\% = \pounds 280$$

Calculation of Total Excess Profit Amount

In accordance with 3.3.3(ii), the Total Excess Profit Amount shall be the sum of all individual Excess Profit Amounts calculated for each applicable Band. Therefore, the Total Excess Profit Amount shall be calculated as follows:

Band 1 Excess Profit Amount + Band 2 Excess Profit Amount + Band 3 Excess Profit Amount + Band 4 Excess Profit Amount

$$= \pounds 105 + \pounds 175 + \pounds 280$$

$$= \pounds 560$$