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Briefing on the New Horizon Contract

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1. Introduction

This paper is prepared as a summary of the main differences between the old and new contracts between POCL and ICL Pathway, following the cancellation of the benefit payment card, and the new commercial terms agreed by the Post Office Board on 24 May 1999. The intended audience is POCL managers who need to understand the main provisions of the contract, either because they have working contacts with Pathway or because they have an interest in the services Pathway will be delivering under the new contract.

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2. The New Contract

Background

On 24 May, 1999 Post Office Counters Ltd and ICL Pathway signed a letter agreement that made major changes to the previous contracts between POCL and Pathway. At the same time, DSS and ICL Pathway agreed to terminate their contract for the benefit payment card services, and DSS withdrew from the tripartite Authorities Agreement.

The letter agreement specified that POCL and Pathway should produce a "codified" contract that incorporated the changes into a new contract by 16th July. The codification process has now been completed, and the new contract is due to be signed on 28th July.

There are significant changes to many aspects of the contract, summarised in the following sections.

Service Scope

The new contract excludes all the services that Pathway were due to provide in connection with the benefit payment card, but includes order book control service throughout the contract.

The software-related services to be delivered at the contracted price are restricted to those defined in the baselined versions of the Release Contents Definitions (RCDs) for the Core Services Release and the Core Services Release Plus. This includes dealing with agreed qualifications to the CSR+ RCD. Any other software-related services would have to be introduced by POCL through change control and would be at additional cost.

The Core Services Release (CSR) is broadly equivalent to NR2 under the old contracts, minus the benefit card related services. The Core Services Release Plus (CSR+) is the replacement for the old NR2+, and includes Logistics Feeder Service, Watercard and Quantum.

The number of counter positions to be automated is limited to 39,750. (Previously this was 40,250, with price increases for any above 38,750). The 39,750 includes positions in training centres - which are no longer subject to a separate limit - and includes up to 250 portable configurations. The contract clarifies that these are notebook computer based; standard equipment mounted on trolleys etc. does not count as mobile configurations for this purpose. In addition to the counter configurations, up to 1,000 post offices can have back-office PCs.

Carrying out the data migration procedures in outlets is now a POCL responsibility; a price reduction was built into the charges to compensate for this.

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Prices

The basis on which POCL pays for services under the contract is entirely different, and is modelled on standard "turnkey" build and operate contracts, rather than on the PFI basis of usage-based charging.

There are two main elements of charging for the contracted services:

- Stage payments on Acceptance and during roll-out
- Operating payments during the steady-state operation of the services.

These charges are largely fixed - 7% of the operating payments is variable by the number of transactions, and a further 32% is variable with the number of post offices at which the service is provided.

In addition, there are specific charges related to modification costs during the roll-out, though these are the resolution of a long-standing dispute about liability for modification costs, rather than a new feature in the new contract.

Any changes or additions to the contracted services will be charged on a time and materials basis, either through contract change control, or through the Operational Business Change catalogue which will set out pre-defined prices for various types of outlet change.

In addition to the charge-out rates applicable to Pathway development staff, senior consultants' and senior managers' involvement in changes is now chargeable at higher rates than other Pathway staff.

The previous allowances of 1.6% offices opening or relocating and 1% closing per annum built into the standard charges still apply, and will be provided as a refund at the year-end, based on the most expensive changes during the year.

All charges will be subject to usual invoicing procedures, but there is a shorter timescale (23 days rather than 30) for payment of invoices for the stage payments during roll-out.

Risk Transfer

The new contract significantly reduces the risks that Pathway was previously taking under the PFI. In particular, risks in relation to achievability by POCL of the roll-out timescales and in relation to future business volumes are now largely with POCL. Pathway's risk in connection with fraud is also reduced, largely as a result of removal of the payment card from the contract.

If POCL delays the roll-out timescale, then Pathway is entitled both to receive stage payments as though the delay had not occurred, and to have a time and cost adjustment for any over-run of roll-out activities.

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Timescales

The new contract will run to March 31 2005, unless terminated earlier by POCL.

The main roll-out is to start on 23rd August 1999 and be completed by 5th February 2001, with a peak rate of 306 offices per week during 2000. 730 post offices are expected to be left outstanding at the end of the main roll-out. These are to be handled through operational business change, but at no additional cost to POCL, and are planned for completion by 14th May 2001.

The planned date for the CSR+ release is April 2000.

Acceptance

Contractual Acceptance only applies to the Core System - i.e. the release of software and other associated services that is being delivered in the Live Trial and for the start of roll-out. There is no provision for Acceptance of CSR+ or subsequent releases (though all releases are subject to testing and release authorisation). The thresholds for medium severity Acceptance faults have been increased from 10 faults in total, to 20 faults overall, or 10 in any one Acceptance Specification. The threshold of any 1 high severity Acceptance fault still applies.

There is a disputes resolution process for any disagreements over the status or severity of acceptance incidents. This involves an expert decision by Peter Copping of PA Consulting (or a replacement with similar skills and seniority) with POCL having certain defined grounds for vetoing such decisions.

Contract Structure

There is now a single contract, rather than the three contract structure that applied previously. The organisation of the contract into clauses and families of schedules has largely been preserved, with those schedules in the old Authorities that are still relevant having been merged into the corresponding schedules from the POCL Agreement.

The Schedules are organised as follows:

Schedule 1

This is an overview of the POCL service environment with which Pathway's services are expected to work.

"A" Series

These include the main "terms and conditions" schedules, and the Requirements and Solutions. A new schedule has been added which defines how Change Control Notes and Change Requests that were signed but not incorporated into the old contracts, or still in progress, will be carried forwards into the new contract. A copy is at Annex 1.

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"B" Series
These are the Contractor schedules and include the Hardware Software and Documentation licensed for use by POCL, Interface validation procedures, the contractual Timetable, and rules for aggregation of any remedies resulting from failure to meet transaction time service levels.

Schedule C1
This lists Optional Services that Pathway will provide on request at additional cost to POCL.

"L" Series
These set out obligations in relation to the Operational Trial

Functional Schedules
Each series covers one of the contracted services, including service definition, acceptance, roll-out, POCL responsibilities, service management, service levels, contingency services as follows:

Series	Service
E	Automated Payments
F	EPOS
G	Infrastructure
H	Order Book Control
K	Logistics Feeder

Contract Controlled and Contract Referenced Documents
The current list of Contract Controlled and Contract Referenced documents is at Annex 2. These form part of the contract. Documents that related to the DSS services, infrastructure and roll-out and to BES in the old contracts are no longer a part of the contract (with the exception of the CCD covering benefit card exit arrangements.)

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Precedence
The precedence of the components of the contract has been changed in the new agreement. This is relevant in the event of any conflicts between different provisions of the contract. The general order of precedence is:

a. Clauses and Schedule A1
b. Schedules A2-A14 and A17
c. Schedules E1, F1, G1, H1, K1 (Service Definitions) and G6 (Infrastructure Roll-out)
d. Schedule A15 (Requirements)
e. Schedule A16 (Solutions)
f. Other Schedules
g. Contract Controlled Documents (CCDs)
h. Contract Referenced Documents (CRDs)

There are two exceptions:
1. In relation to service levels, the Service Level schedules (E8, F8, G10, H8, K8) take precedence over everything except the Clauses and Schedules A1-A14 and A17.
2. In relation to software-related services, Pathway's obligations are limited to those in the CSR and CSR+ release contents definitions. (Even though these are CCDs and would normally rank below the requirement and solutions, they are given precedence in this regard by a specific reference in the Clauses.)

Contract Management
The new contract includes changes in the meetings and procedures for commercial and contract management of the POCL-Pathway relationship. In particular it sets out new procedures for change management.

The contract defines 6 joint management processes for contract management. These are:

Change control - this is now to be overseen by a joint change control board, meeting fortnightly, which will agree timescales, monitor progress and review decisions. Changes will (subject to authority limits) be able to be authorised by the Head of Horizon Commercial for POCL and by the Finance and Commercial Director for Pathway. There are also urgent and emergency procedures for changes that can not wait for the normal timescales. Pathway will not carry out any changes without a validly authorised CCN. The backlog of CCNs from the Related Agreements is to be cleared by December 1999.

Contract Administration - this formalises the role of the POCL and Pathway Contract management teams in maintaining an up to date version of the contract and in providing expert guidance on the preparation of CRs and CCNs, and monitoring resolution of agreements to agree.

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Service Review Board - this is unchanged from current arrangements.

Contract Steering Group - this is a new meeting which takes over the roles which were fulfilled under the old contracts by the Joint BA/POCL/Pathway Contracts Negotiation Team (CNT) and the POCL/Pathway Commercial meetings. It is the escalation route for issues from the change control and contract admin. areas, and also for any disagreements about Remedies from the service review.

New Business Board - this is a reinstated meeting that will oversee new developments during the pre-contract stages when requirements and solutions are developed through the Business Requirements Definition process.

Release Authorisation Board - this has the same role in relation to CSR, CSR+ and future releases as similar boards have fulfilled in the past.

The previous disputes resolution procedures in the contracts have been removed. In the new contract, other than in relation to Acceptance, any dispute that can not be resolved in negotiation between POCL and Pathway is subject to the courts.

Termination and transfer

POCL can, as before, terminate the contract by giving 12 months notice and paying a termination fee based on Pathway's unrecovered costs and lost profits. In addition POCL can terminate in various circumstances where Pathway is in default without paying compensation. As previously, there is no provision for early termination by Pathway.

On cessation of the services from Pathway - either at the end of the contract or on earlier termination - POCL has an option to purchase the project assets (i.e. the hardware, software licences, telecommunications contracts etc.) Following completion of roll-out, or any time if POCL pays the termination charge, the cost is one pound; prior to that the cost represents Pathway's unrecovered investment in hardware.

Future Developments

All future developments on the infrastructure are to be agreed through change control. POCL will have the choice - on a case-by-case basis - of contracting for developments at a fixed price or on a time and materials basis. Operating charges for additions to the service will be at marginal cost for services developed for Royal Mail, DVLA, DNS, Girobank, and the Co-op Bank. Operating charges for products for other clients or for POCL's own applications are to be agreed, and may be above marginal cost.

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POCL and Pathway will resume and continue discussions on establishing a Public Private Partnership for developing network banking and government gateway services on the infrastructure. However, such a partnership is not yet in place and there is no obligation on either side to agree to one being established.

3. Implications of the New Contract

Introduction

The cancellation of the payment card, and the new commercial terms with Pathway mean that POCL managers need to adopt a different approach in dealings with Pathway to those that were applicable under the old regime of a PFI contract and joint sponsorship with DSS.

The new situation brings significant challenges for POCL:

- the new contract with Pathway is more costly and involves large up-front payments, thus putting pressure on both cash-flow and profitability; and
- loss of the benefits card means both the loss of a stream of income from BA and puts at risk a third of POCL's existing business, with the planned move of benefits payment to automated credit transfer within the life of the Pathway contract.

This means that POCL needs to maintain tight control of expenditure with Pathway and maximise the business benefits from the core system services which they are contracted to deliver at a fixed price.

Cost Control

There are two elements to this.

Firstly, all POCL managers need to ensure that they deliver the POCL responsibilities under the contract for which they have responsibility. This is particularly important in regard to any activities which could affect the roll-out timescale, since any slippage which is (wholly of partly) POCL's responsibility will result in increased payments to Pathway.

Secondly, any changes are likely to result in additional charges. The presumption must therefore be against change - i.e. the business priority is to deliver and exploit the core functionality that POCL will get at the contracted price.

Changes can only be introduced through the change control procedure using a Change Request. There is no central budget for changes and therefore any change requests that involve chargeable work by Pathway need to include a business justification and budget provision - these will be confidential to POCL and should not be shown to Pathway without clearance from the Horizon commercial team.

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The detail required for the business justification will depend on the costs involved. For minor changes that can be accommodated within existing budgets, a simple statement of benefits would be sufficient. Larger changes would require authorisation through the usual business control processes via CoMPEC and/or MaPEC.

Typically budget provision will either be in the form of sponsorship from the business customer for the change (e.g. from the client account manager in the case of new automated products) or provision from an existing budget (e.g. if a manager in Horizon is able to reduce their budget by making savings on their consultancy budget by paying Pathway to do work that was previously budgeted to be done in the Horizon Programme).

Change Management

POCL will need to implement internal management processes to support the new contractual change management process. This is overseen by a joint change control board, and where changes are contentious or particularly costly, the change sponsors may be asked to attend to help resolve the issues arising.

Because of the new liabilities for delay, it is essential that POCL meets agreed timescales for reaching decision on proposed changes. This includes review of associated documents. Timescales will be agreed in advance at the joint change control board meetings which will take place on a fortnightly cycle.

4. If You Need More Information

Reading this document is not a substitute for getting expert advice on specific issues, on which you should contact either the Commercial or Contracts team for advice. (Liz Blackburn on GRO on commercial issues, or John Cook on GRO on contracts issues.)

The whole of the contract , with the exception of the pricing schedule, which is commercially confidential, will be made available to Horizon programme staff on the LAN once it has been agreed by John Roberts and Neville Bain. In the meantime, I will hold a printed reference copy in King Edward Building.

The contract is a lengthy and complex set of documents and you are advised to seek expert guidance (as above) before relying on any parts of it, since there are complex interdependencies, definitions, and rules of precedence that may affect its meaning.

KEITH BAINES
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27th July 1999