

Post Office

BA/POCL - UPDATE FOR THE PRIME MINISTERWhat option have we been exploring with ICL?

Since last week, we have been exploring with ICL whether we might find a way forward for the Horizon project in which the Post Office would buy the basic ICL hardware. This would provide automation at post office counters for services like bill paying and postage rates, and a platform the Post Office could build on to win business. The plan would be that the Benefits Agency would use ACT to pay benefits into accounts in High Street banks. The Post Office would offer cash back facilities based on access to these accounts. The arrangements would provide a basis for network banking (under which the Post Office would provide customer services for High Street banks). It could also provide a smartcard for Modern Government services. The system would provide a new capability to combat benefit fraud.

What progress have these discussions made?

Discussions with ICL have foundered on two fundamental issues:

First, contractual issues. Three key points here:

- ICL want unconditional agreement today. They say this is necessary if they and Fujitsu are to avoid a provision in their accounts. But the consequence of this is that, if unforeseen terms and conditions came up in the substantial process of moving from the present outline agreement to full contracts, the public sector would have no right to withdraw. Entering a contract on this basis would be unusual and, if there proved to be costly surprises, subject to criticism;
- ICL are not prepared to allow part of the contractual payment to be dependent on the system performing satisfactorily when fully rolled out. This means the Post Office could pay for a system which did not perform as necessary;

- ICL are not prepared to give evidence of ownership of the assets involved, or to give perpetual licences for all the IPR. This means the Post Office could find that, when the system is installed and operating, the IPR is owned by a third party. Such a third party would be in a strong position to drive a costly settlement with the Post Office.

Second, we are far apart on the price. We believe that the best test of whether any price is reasonable is to compare it with the cost of terminating the existing contract and purchasing comparable hardware and associated services from an alternative supplier.

Even after a late movement by ICL last night, ICL's offer still represents considerably worse (the gap is around £100 million) value for money compared with the option of going to an alternative supplier. This is based on the assumption that we would need to pay £150 million to ICL to settle the termination (Treasury Solicitor agree with this assumption) - if the number were larger, so the gap between the ICL offer and the alternative would reduce.

But even if there was further movement from ICL on the price (and the signs are that significant movement is unlikely), the contractual issues - in particular that of conditionality - are showstoppers in their own rights.

What are the alternative options?

At the moment, there seems no alternative to termination:

- ICL have withdrawn their December 1998 offer to proceed with the original Benefit Payment Card (Option A). This Option is therefore effectively dead;
- The B1 option (in which the Post Office would create benefit accounts accessed by a smartcard) has an even worse value for money gap (£300 million) compared with termination. And the same problems on conditionality would also apply.

Way forward

If termination is the only realistic option, the key must be to ensure that we move as swiftly as possible to negotiations on a termination settlement, while protecting the public sector's legal position. Ideally, we would have a public line, agreed with ICL, for use during this time, but we have prepared a media handling strategy for whichever way these termination discussions go.

But at the moment, discussions with ICL have not broken down, and we must avoid saying anything now that precipitates such a breakdown. We therefore advise no change in the lines to take (attached). However, Keith Todd (ICL) is meeting Alan Milburn and Stephen Byers at 10am today, and we will advise further in the light of that meeting.