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HM Treasury  
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Post Office Counters Ltd

11 December 1998

Dear Sarah

SARAH GRAHAM'S LETTER

Having just had sight of Sarah Graham's paper with its attachment from George McCorkell I have a number of comments to make:

MAIN TEXT PARA 3

Sarah has suggested some wording on Alternative Options. I support the broad thrust of the statement with the exception of the last sentence. I believe it would be misleading Ministers to suggest the possibility of a better VFM case for Options 2 and 3. POCL has already outlined its position formally to Ministers on Option 2. On Option 3, POCL has made it clear that this is not a realistic option as currently defined. We have no means of knowing if KPMG numbers will be borne out in reality both in terms of stability of the network or the costs of automation, profits from Banking etc.

It is also quite possible that in achieving VFM, the NPV effect on one or other (ie, BA or POCL) could be significantly improved/worsened eg by deferring ACT or the impact of interim Banking on POCL's profits. I suggest therefore the last sentence should read:-

"However all parties are committed to working together in a pro-active manner against a clearly defined set of objectives to fully maximise the value for money from alternative options to Horizon".

ATTACHMENT ON DSS REACTION TO ICL PROPOSAL OF 9 DECEMBER

Re: para 3, I had an action point from The Horizon Progress Tracking Group to clarify this point with Hambros.

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I raised this issue at a meeting yesterday afternoon with James Stewart of SG. He confirmed that Fujitsu were prepared to stand behind the whole project, ie up to whatever funding is required. The reference to £600m in Keith Todd's letter to the Chief Secretary was meant to emphasise the scale of investment - not set a cap on it.

He also confirmed that Fujitsu's support for this programme would be similar to that provided for DTI project Elgar - but made the point that the letter of support for that project (provided at preferred bidder status) had yet to be converted into legal terms. I believe this covers the point made by George McCorkell at the meeting yesterday. James Stewart also advised that Adrian Montague has been fully briefed by ICL on the nature of Fujitsu's support.

Clearly BA and POCL would need to ensure that Fujitsu's support for Horizon was expressed in legally enforceable terms as part of any agreed way forward.

(i) Commercial

Para 4.1 should read: On 9th November 1998, ICL were seeking price increases which would increase the NPV provided under Corbett from £116m to £237m +£80 contingency to be funded by the public sector. They are now seeking price increases to increase the NPV from £116m to £229m and the contingency fund has been removed. Conclusion: they have moved £88m from their 9 November proposal.

(ii) Acceptance

The Acceptance tests do not relate solely to system tests. There are tests which will involve live running. However, POCL do share BA's view that a full live trial is necessary.

(ii) *EFFECT OF LATEST ICL PROPOSAL ON DSS COSTINGS FOR OPTION 1*

Para 3: I note George's estimate of the impact on BA of the revised programme timescales.

As a counter balancing effect I think it is worth pointing out that in view of revised BA volumes and ICL's latest pricing proposals BA's charges from Pathway are significantly lower than originally envisaged when the programme was tendered for. (I believe Keith Todd has suggested a figure of £107m lower in his letter to the Chief Secretary).

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In the interests of speed I have made some manuscript amendments to George's table to reflect a more rounded position on ICL's latest proposal.

If you have any queries please give me a call.

Yours sincerely

**GRO**

Mena Rego

cc Sarah Graham  
Ross Newby  
George McCorkell  
David Sibbick/Isabel Anderson  
Geoff Mulgan  
Andrew Montague  
Joseph Haligan  
Jeremy Crump  
Peter Schofield

**FUNDING**

CORBETT	9 NOV	9 DEC
FUJITSU GUARANTEE ICL BORROWING (£600 Million)	GOVT GUARANTEE ICL BORROWING	FUJITSU SUPPORT ICL FUNDING THE PROJECT. NOT CLEAR IF THIS CAN BE ENFORCED.
OPTION TO PURCHASE SYSTEM ON TERMINATION	OBLIGATION TO PURCHASE SYSTEM ON TERMINATION	OBLIGATION TO PURCHASE SYSTEM ON TERMINATION IF IT HAS VALUE.
CAP ON LIABILITY IF GOVT TERMINATE	<del>NO CAPPED AT AGREED</del> BORROWING + EQUITY	<del>NO CAP</del> CAPPED AT AGREED BORROWING + EQUITY.

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# COMMERCIAL

	CORBETT	9 NOV	9 DEC
NPV OF ADDITIONAL PAYMENT TO ICL	£116m	<del>£317m</del> * £237m	£229m
ICL ESTIMATED <sup>NPV</sup> LOSS	£224m	£103m	£118m
RPI LEVEL BEFORE PRICES INCREASE	6%	2%	2%

Guarantees

75%

80%

75%

\* This figure includes £80m provision for contingency.

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## ACCEPTANCE

CORBETT	9 NOV	9 DEC
LOSE TERMINATION RIGHTS ON SUCCESSFUL COMPLETION OF SYSTEMS TESTS AND <u>LIVE TRIAL</u> (CB ONLY)	SYSTEM TEST ONLY	<del>SYSTEM TEST ONLY</del> BASED ON COMPLETION OF 24 ACCEPTANCE TESTS (SOME OF THESE CAN ONLY OCCUR IN LIVE RUNNING)
GUARANTEE PAYMENT APPLY ON ACCEPTANCE AND ROLLOUT OF ALL CONTRACTED FUNCTIONS	APPLY ON SYSTEM TEST ONLY NO ROLLOUT (CB ONLY)	<del>APPLY ON SYSTEM TEST AND ROLLOUT (CB ONLY)</del> APPLY FROM 30 SEPTEMBER ASSURING SUCCESSFUL COMPLETION OF LIVE TRIAL
NO MORE THAN 10 CATEGORY 'B' FAULTS	NO MORE THAN <u>230</u>	NO MORE THAN <u>100</u>
INDEPENDENT EXPERT TO FACILITATE DISPUTE RESOLUTION	EXPERT MAKES BINDING DECISIONS	EXPERT'S DECISION MUST BE IMPLEMENTED. GOVT CAN LATER SEEK REDRESS IN LAW

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