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Rww/1/05.

To:
MR JOHNSON

ci: *Secretary of State
*Sir Michael Scholar
*Mr Macdonald
Mr Davis CGBPS
*Mrs Britton PORT
*Mr Hosker FRM
*Mr Osborne Legal C
*Mr Tee NEWS
*Mr ~~Brebn~~ PORT
*Mr Leese PORT
*Mr Whitehead CGBPS 1
*Ms Anderson CGBPS1
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From:
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6 August 1999

* without attachments

HORIZON PROJECT AND THE FUTURE OF POST OFFICE COUNTERS NETWORK

1. Simon Lancaster's minute of 4 August provides helpful feedback on your reactions to the briefing we have so far given you on Horizon and Counters issues, and asks some further questions. This note deals with the latter in turn, and suggests some further follow-up.

Priority 1: Future Income of the Post Office

2. The longer term future (the income from the Benefits Agency will begin to diminish seriously only from 2003) of the post office counters network and how it is to be funded has been the subject of several rounds of Ministerial correspondence, of which I attach copies at Annex A. It was out of this correspondence that the suggestion for an interdepartmental study undertaken by the PIU emerged (the suggestion to involve the PIU came specifically from Geoffrey Norris at No. 10). The position on that study is that the PIU Selection Panel have included it as their number one priority for their programme of second generation studies starting this autumn. This programme has been put to the Prime Minister for approval, which is still awaited. It would, however, be very surprising if the Prime Minister rejected the recommendation. In the meantime, though, we should say nothing publicly, though Mr McCartney has shared what I have said above with members of the Horizon Working Group on a confidential basis.

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3. The basis for asserting that 50% of the network could close as a result of the decision not to proceed with the Benefit Payment Card comes from Post Office modelling. John Roberts said it publicly at the recent press conference to launch the Post Office's 1998-99 Report and Accounts. Very broadly, the Post Office have assumed that all those offices where the fixed element of the remuneration package makes up more than 50% of the subpostmaster's total remuneration would be vulnerable to closure if the network as a whole lost profitability. The argument is that those offices where the fixed element represents less than half the total remuneration are subsidising those where it represents more than half. If the network as a whole lost profitability, the funds to sustain this cross-subsidy would no longer be available. Without the high levels of fixed payment these offices which depend on them would no longer be viable and would close.

4. In practice, of course, some of these offices would not close. But those that did not would be offset or more than offset by offices, particularly those in deprived urban areas, which at present transact high volumes of Benefit Agency work, and whose volume-related payments are therefore well above the 50% threshold. These volume related payments would be decimated following the disappearance of BA work. The effects on the ground are shown graphically in the series of four maps which accompanied Ian McCartney's letter of 7 July to the Chief Secretary (included in the exchange of Ministerial letters at Annex A - the maps are attached separately).

5. The Post Office do, however, have an increasingly refined computer model of the network (KPMG made extensive use of it during the Horizon negotiations), and if you would like a more detailed assessment of how the progressive loss of income from the Benefits Agency is expected to impact on the network, I suggest that we ask the Post Office to take you through this after the summer break.

Priority 2: Post Office/Government Relations

6. I attach at Annex B an earlier submission to Mr McCartney which sets out more fully at paragraphs 5 to 8 the outstanding issues between POCL and BA. Since that was written, the two sides appear to have narrowed their differences on acceptance testing, and it seems likely that the issue of floor payments could also be solved quickly if a solution on the third issue, payments for OBCS, could be found. Since that submission was written, there have been discussions between Lord Falconer and Alistair Darling, and between Lord Falconer and Mr McCartney. (However, the meeting between Mr McCartney and Alistair Darling, for which the submission was prepared, failed to take place).

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7. The result of these discussions appears to have been that Alistair Darling insisted that he has no room in his budget to accommodate additional payments to POCL, and that Lord Falconer and Mr McCartney concluded that the next step might be a discussion with the Chief Secretary.

8. You ask how this might now be taken forward. I spoke yesterday to Geoffrey Norris at No 10, and pressed on him the need for an early resolution of the issue. I suggest however that what we really need is for Lord Falconer to pick this up again, and to try to broker a deal which would probably need to involve Alistair Darling, Alan Milburn and yourself. I suspect it will be difficult to make progress now until Ministers return in September. Alistair Darling is, for example, now in the United States, and others will no doubt either have already left for their holidays, or will very shortly do so.

9. When you meet Neville Bain and John Roberts next week, I suggest that you should re-assure them that we have not given up on trying to get for them a better deal than is currently on offer from BA, but that we are unlikely to make much further progress until Ministers return in September.

10. Given DSS's vast overall budget, it is hard to believe that they could not accommodate at least some modest improvement to their offer on OBCS to POCL. I have of course pressed my colleagues in DSS on this; but both they and HMT officials agree that the issue now rests with Ministers for decision.

Priority 3: Payment of Benefits in Cash

11. The Post Office can of course already offer benefit recipients who choose to be paid by ACT the facility of collecting the benefits in cash at post offices. All that is needed is for the benefit recipient to open an account with Giro Bank, the Co-operative Bank, or Lloyds TSB.

12. At present however, this agency work carried out by the Post Office on behalf of the three banks is based on slow and expensive paper transactions. This way of doing business could not possibly cope with a huge influx of new accounts from benefit recipients. Two developments need first to be put in place.

13. First, the Horizon Platform needs to be completed and rolled out to every post office in the network so that transactions can be conducted electronically and on-line; and second, the Post Office needs to secure agency deals with a wider range of retail banks and building societies. The clear objectives are to have the Horizon platform fully rolled out throughout the network by end March 2001, and for an extensive range

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of agency agreements with banks and building societies to be in place before the migration of benefit recipients to ACT begins in 2003.

13. We plan to invite the Benefits Agency (Alastair Darling has given his agreement to this) to an early meeting in the autumn of the Horizon Working Group which you will chair, so that they can explain their strategy and time table for the migration to ACT. One area of particular interest will be how the minority of benefit recipients (perhaps as many as two million or so) who do not want a Bank Account or would not be suitable to be given one, are to be accommodated by the Benefits Agency within the Government's pledge to ensure that all benefits recipient who wish to do so will continue to be able to draw their benefits in cash at post offices.

Finally.....

15. I am grateful to Simon for sending me copies of various helpful background reading including your speeches last year to the New Statesman Conference and the Postal Strategy Conference. I will copy these more widely to colleagues here.

DAVID SIBBICK