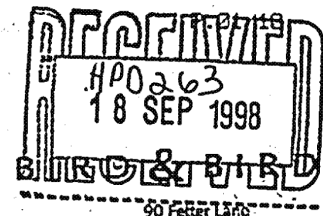


18-SEP-1998 12:10 FROM BIRD & BIRD

TO 97763955



FAX TRANSMISSION

To: POCL

Atten/Ref: Pat Kelsey, Head of Contracts

CC: Joe Ashton, PO Legal Services
Andrew Davies, Project Mentors
Sarah Graham, DSS
George McCorkell, BA
Dave Miller, Horizon
Ron Powell, DSS
Mena Reno, Horizon
David Sibbick, DTI

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From: Hamish Sandison

Matter: BPOCL-001

Account No: BPOCL-001

Date: 18 September 1998

Number of pages (including this page) :

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Message:

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*not a solicitor

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P.02/10

3. I attach an outline negotiating brief. I stress that it is only an outline, and that further work is required to put flesh on the bones. However, I hope that it will serve to move our discussions forward.

4. If my outline is acceptable, and subject to any comments you may have, I believe the next steps that must be taken in order to produce a detailed negotiating brief are:

- (1) to secure the agreement of BA and POCL [DQ: and the DTI? HMT? PU? George Corbett ?] to the outline negotiating brief;
- (2) to invite George McCorkell (for BA), Mena Rego (for POCL) and yourself (for the joint BA/POCL Programme), to contribute more detail in their respective areas on the substantive issues; and
- (3) to achieve an agreed common position between the public sector lawyers on the legal parameters for the negotiation (I understand that a meeting of the public sector lawyers under Elizabeth Hambley's chairmanship has already been proposed for this purpose).

Steps (1) and (3) can of course proceed in parallel.

5. Until this detailed negotiating brief is agreed by both BA and POCL, I would strongly advise both of my public sector clients not to commence substantive negotiations with ICL.

RAB-BPOCL001MEMO-KELSEY.M17

[DRAFT/18.09.98]

OUTLINE NEGOTIATING BRIEF

INTRODUCTION

1. Describe the purpose and scope of the negotiating brief: to set out the substance of the agreed public sector position and the process for carrying it forward.

A. SUBSTANTIVE ISSUES

2. Summarise remit for negotiations as set out in paragraph 3 of Stephen Byers' letter and attached terms of reference (10 September 1998):

- To establish whether there is a commercial basis for proceeding with the project which is acceptable to the parties;
- To resolve outstanding differences on project implementation and timetable; and
- To identify any further action which would need to be taken to ensure successful delivery of the project [DQ: Is this an issue for the negotiating strand or for the working group?]

3. Rcafirm the agreed legal basis for negotiation, namely, that:

- ICL is in breach;
- the public sector parties are entitled to terminate and claim damages; and
- the public sector parties reserve the right to terminate and claim damages if a commercially acceptable basis for proceeding cannot be agreed between all the parties.

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TO 97763955

P.04/10

4. Set out the agreed legal parameters for negotiations: as recognised in Stephen Byers' letter to ICL Pathway (15 September 1998), any adjustment to the contracts must be compatible with procurement law. In particular, as emphasised in Alistair Darling's letter to Stephen Byers' (September 1998):

- the contract cannot safely be carried on beyond 2007;
- the prices cannot be significantly increased [DN: Consider appending agreed statement of the procurement law position]

5. Set out agreed commercial parameters for negotiations:

- the contract must provide a firm date after which BA will have no further commitment to using the benefit payment card (see Stephen Byers' letter to ICL dated 15 September 1998 at paragraph 4);
- the DSS's ability to migrate to an ACT-based system, in preparation for the end of card usage by contract end date, must be transparent to ICL (see Alistair Darling's letter to Stephen Byers dated September 1998 and Stephen Byers' letter to ICL dated 15 September 1998 at paragraph 4, second bullet);
- [DQ: Anything else?]

6. Set out any areas where ministers/public sector parties are prepared to compromise and the degree of compromise they will accept. For example:

- More money for additional services?
- [DQ: Any other ideas?]

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7. Other currently outstanding issues: these must be resolved as part of any overall settlement with ICL. They include:

- For BA: see Pat Kelsey's letter to me dated 15 September 1998 [copy attached];
- For POCL:
 - The counterspace dispute;
 - [DQ: Any other outstanding issues?].

B. PROCESS

8. Reconfirm that negotiations will be conducted in accordance with the terms of the standstill agreement. This means (inter alia) that:

- Negotiations are without prejudice;
- Negotiations are confidential;
- No party will sue any other party while negotiations are continuing.

9. Establish the timetable for concluding negotiations and reporting back to ministers, i.e., no more than one month.

10. Describe role of the adviser ("troubleshooter"): see terms of reference attached to Stephen Byers' letter to ICL dated 15 September 1998.

11. Specify membership, roles and responsibilities of the public sector negotiating team: see attachment.

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[DRAFT/ 18.09.98]

Membership, Roles and Responsibilities of the Negotiating Team

Role	Individual	Responsibilities
Adviser ("Troubleshooter")	Graham Corbett	To facilitate discussions and report to ministers via the Chief Secretary to the Treasury
Lead Negotiator	[to be advised]	Leads negotiations on behalf of both public sector parties
Lead Legal Advisor	Joint Programme Lawyer (Hamish Sandison)	Represents legal interests of joint contracting authorities
Lead Negotiator (BA)	[to be advised]	Leads negotiations for BA
DSS Representative	[to be advised]	Represents DSS' interests
Lead Negotiator (POCL)	[to be advised]	Leads negotiations for POCL
DTI Representative	[to be advised]	Represents DTI's interests
BA Legal Advisor	[to be advised]	Represents BA's legal interests
POCL Legal Advisor	[to be advised]	Represents POCL's legal interests
Contracts Manager	Joint Head of Contracts (Pat Kelsey)	To provide technical support from the joint contract management team

NOTES:

1. The Joint Programme Lawyer would expect to be supported by one assistant solicitor (for drafting) and one trainee solicitor (for note taking).
2. Other team members would expect to call in specialist support as required.

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P.07/10

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Direct Fax: **GRO**

Hamish Sandison
Bird & Bird
Fetter Lane
London

15th September, 1998

Dear *Hamish,*

Commercial and Contractual Issues

We discussed your conversation with George McCorkell who requested that I write to him about outstanding commercial and contractual issues. I produced a DSS specific paper on 16 July and I have been asked to send a copy to you. The document is attached and I should be grateful if you would provide a copy for George McCorkell at the meeting I understand you are having tomorrow.

I think it is important that we do not forget the POCL issues and would want to discuss how we factor these in. I think it is important also to share the paper work with both Authorities. I await your comments.

Yours sincerely

GRO

Pat Kelsey
Joint Contracts Manager



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Document 2

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RESTRICTED COMMERCIAL/MANAGEMENT

COMMERCIAL AND CONTRACTUAL ISSUES

1. INTRODUCTION

1.1. There are outstanding commercial and contractual issues which need to be addressed during any negotiations on the continuation of this programme. These are listed below with the information known to the Joint Contracts Team. There have been no discussions with sponsors on any negotiation brief to be used.

1.2. In addition information is provided on the revenue guarantees in the Related Agreements and the factors that may affect them..

1.3. This paper is written in respect of DSS only.

2. COMMERCIAL ISSUES

2.1. CCN105

2.1.1. There are two issues outstanding from CCN105:

- CAPS dates;

Contractual arrangements state that should CAPS fail to meet its milestones, resulting in delay to Pathway obligations, the end of the contract will be extended on a day for day basis. The CAPS dates in question are around direct interface testing on CAPS 2.2 and 3.0. These dates have been and remain in dispute. In addition, Pathway do not now accept that there has to be a consequential delay in delivery of their obligations.

- Charging structure

This is covered in section 3 below.

2.2. Benefit migration

2.2.1. Pathway have raised issues about changes (originally presented over a year ago) to the Department's benefit migration plans. They point out that these refer to costs incurred and do not allow for margin lost on scorecard revenues foregone. The areas in dispute cover help desk, cards, and customer education. By far the largest cost is in the area of customer education, in particular the Department's requirements for payment advice notices (PANs). The total costs claimed for all areas are between £4.3 and £12.7 million, dependant upon chosen scenarios. These areas remain unresolved, with the understanding that they would be concluded in the current replan negotiations.

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2.3. Other areas

2.3.1. There are several other areas that are likely to be significant in negotiations, although we have not yet a defined sponsor position, nor formed a view of Pathway's commercial stance - all sides would expect to cover them in any negotiation:

(a) Acceptance

we need to be clear at what point we grant acceptance and forego termination rights for failed acceptance;

(b) Guarantees

section 3 below sets out the current position, but there may be need or opportunity to vary the levels and conditions related to guarantees dependant upon the content of various releases. NB the guarantees are also affected by the CCN105 dispute explained in section 3 below;

(c) Remedies and liabilities

there may be a need to vary these dependant upon the content of releases and the effect of faults or deficiencies.

3. CHARGES AND GUARANTEES

3.1. Guarantees

3.1.1. This section sets out the position on DSS revenue guarantees as at the conclusion of CCN105 (the current contracted position, assuming rollout starts in November 1997). In calculating the figures, the following assumptions have been made:

- that all CAPS dates are met;
- DSS volumes never reach the point to exceed guarantees;
- consequential effects of POCL volumes are not allowed for in the BES figures.

£m	97/8	98/9	99/00	00/01	01/02	02/03	03/04	04/05
PAS/CMS	0.12	24.95	57.81	64.69	59.52	53.75	48.29	42.94
BES	0.34	20.32	32.34	34.75	31.58	28.58	25.75	22.90
Total	0.46	45.27	90.15	99.44	91.1	82.33	74.04	65.84

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3.2. Factors that could affect charges

Provisions in the charging schedule

(a) RPI Indexation

The schedule allows for an increase in charges (both service point based and guarantees) in the event that the RPI increases by more than 6% in any one year. In this event the prices and guarantees are increased by half of the RPI increase. The date of calculation is the last day of February. Hence if, on 28 February 1999, it is the case that the RPI has increased by 10% over the past 12 months, prices and guarantees beyond 1 March 1999 would be increased by 2%.

(b) Benefit frequency changes

The schedule goes on to provide for the effect of changes to the frequency of specific benefit periods. Under the calculation, if a weekly benefit becomes paid four weekly, future volumes of that benefit are multiplied up by a factor of 3.7 in terms of the number of chargeable transactions. Hence if a benefit is paid less frequently there is a small reduction in charges (assuming consistent take up), protecting Pathway's planning assumptions. If it is paid more frequently, the charges would increase by a much lower proportion than the actual volume increase.

CCN105 Charging interpretation

3.2.1. In concluding the consequential contractual amendments arising from CCN105, a difference of interpretation of the effect on the charging schedule emerged. That difference of opinion was acknowledged, documented but never resolved. The PDA and Pathway produced a joint position paper to document the difference.

3.2.2. CCN105 effectively changed the dates of start of rollout and end of contract by approximately 4 months and 2 months respectively. The difference of opinion relates to how the charging periods should be mapped onto the new planning dates.

- Pathway assert that for example, the charging basis for the first period of steady state service should remain the same, even though the dates of that period have changed.
- The PDA asserted that the agreed charging basis is fixed in time, and that as events are delayed they move into different charging regimes.

3.2.3. The difference in the two views represents £7m for the DSS over the life of the contracts.