

15/08 '99 TUE 10:42 FAX

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0001

*Fax to Keith Hardie***GRO***32 pages*Internal *memo***THE POST OFFICE**

To Martin Walsh, David Simpson, Keith Hardie
From Kathryn Hollingsworth
cc
Date 15/06/99

Subject DTI Select Committee Hoaring on Horizon

Please find attached a report, including written submissions, on the DTI Select Committee last night. I hope you find it useful.

Kathryn

15/06 '99 TUE 10:42 FAX
15/06 '99 10:10 FAX

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→ POST OFFICE

002 002

Trade & Industry Select Committee Meeting
14th June 1999

Present:

Martin O'Neill	(Lab, Chairman)
John Butterfill	(Con)
Lindsay Hoyle	(Lab)
Helen Southworth	(Lab)
Roger Berry	(Lab)
Bob Laxton	(Lab)
Alisdair Morgan	(SNP – for only part of the meeting)

Unless stated by a set of initials following the question or the answer, the main questioner is the Chairman and the main respondee is either:

NFSP	Colin Baker
CMA/CWU	Derek Hodgson
ICL	John Bennett
Post Office	John Roberts

(Please see sheet attached)

15/08 '98 TUE 10:42 FAX

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→ POST OFFICE

003

003

TRADE AND INDUSTRY COMMITTEE**LIST OF WITNESSES****ELECTRONIC GOVERNMENT: THE HORIZON PROJECT FOR
AUTOMATED PAYMENT OF BENEFITS THROUGH POST OFFICES****4.15 pm NATIONAL FEDERATION OF SUB POSTMASTERS (NFSP)**

Mrs Jean Kendall	National President, NFSP
Mr John Peberdy	Chairman of Negotiating Committee, NFSP
Mr Colin Baker	General Secretary, NFSP

c4.45pm CMA/CWU

Mr Terry Deegan	General Secretary, CMA
Mr John Loveday	Research Officer, CMA
Mr Derek Hodgson	General Secretary, CWU
Mr Tony Kearns	CWU

c5.15pm ICL

Mr John Bennett	Managing Director, ICL Pathway
Mr George Hall	Director, Corporate Affairs

c5.45pm THE POST OFFICE

Mr John Roberts	Chief Executive
Mr Stuart Sweetman	Managing Director, Post Office Counters Ltd
Mr David Miller	Managing Director, Post Office Network

15/06 '99 TUE 10:43 FAX
15/06 '99 10:11 FAX

GRO

PUBLIC AFFAIRS

POST OFFICE

005

005

Q: Where do you see the Post Offices in 5 years time – any losses?

A: Couldn't put a figure on losses but there are currently 5,000 Post Offices struggling.

Q: Are the main worries the lack of exclusivity? Eg. DVLA getting some electronic services?

A: They do have concerns over the direction that the DVLA is going but they also understand that other parties will want to take advantage of electronic delivery. Also, sees worries that developments could mean a "double-whammy". Not only will money be paid into bank accounts but people will also pay their bills there. PO has been very lucky with utility bills etc. to date.

Q: Do you see any advantage in modernising government?

A: Yes. But who's going to pay for it? Govt wanted to use PPP to provide the service. Post Offices do have worries about use of ATMs etc.

Q: What did you pick up from the trial runs? What did the Post Offices say?

A: No resistance – it was warmly received by user and the Post Office masters. There did seem to be, however, a "Love Affair" with the actual 'book'.

Q: HS: Any view on the interim Barcode system?

A: Very successful – saving £100m in fraud.

Q: Worried about Post Offices vulnerability? Target for crime?

A: PO is being brought up to standard. £40m is being spent on security but it is still not enough.

Q: Any views on how to reduce the amount of cash that the post offices deal with?

A: No. The great attraction of the PO is that it always deals in cash.

Q: What percentage of PO work is benefits related?

A: Est. 25%. 45% if you include Bill payment.

15/06 '99 TUE 10:43 FAX
15/06 '98 10:11 FAX

GRO

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→ POST OFFICE

004

004

National Federation of Sub-Post Office Masters

Chairman: Has anything other than lip service been paid to the idea of the Horizon project?

A: It's easy for the Government to say that they will automate the network of Post Offices but the Post Offices then have to get on and do it.

MO'N: What do you want from ministers? A moratorium?

A: Against compulsory ACT but not voluntary ACT. Problems arise in that not everybody has a bank account- not everybody wants electronic delivery

Q-JB: What about people that do want electronic payment? And Post Offices open on Saturdays?

A: If the economics are right (and have been costed) then Post Offices will not be against offering those services and to opening on Saturday afternoons.

Q: Why are Post Offices not open on Saturdays? Not very profitable then are they?

A-JK: Type of transaction is not conducive to Saturday afternoons. They have found that PO service is superior to that of banks who close earlier than Post Offices and are not open Saturdays.

Q: Once automation is in place, Post Offices will be one way only of getting payment. Will Post Offices be needed?

A: PO will admittedly only be an option. They would like to see a moratorium to try and get a deal going between banks and the Post Offices

Q-LH: Post Offices are backbones of communities. What can Post Offices do to ensure that they get the BA work? People can't open bank accounts for several reasons so they will need Post Offices

A: Post Offices want to make sure that they are still there. They welcome the working group set up under Ian McCartney and want to build on that platform. They feel that social services are carried out in Post Offices everyday and the Post Offices will be looking at ways to improve their service - opening hours, how the PO presents itself.

15/06 '99 TUE 10:44 FAX
15/06 '99 10:11 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

008

006

PAGE 82

12/86/1999 12:19

GRO

NFSP

HP4

THE FUTURE OF THE POST OFFICE NETWORK

SUBMISSION BY THE NATIONAL FEDERATION OF SUBPOSTMASTERS

This submission is made in response to the request from the Select Committee of 9 June 1999 inviting the National Federation of SubPostmasters (NFSP) to give our reactions to the recent announcement by Government of the future of the Horizon project, the events that led to the withdrawal of the Benefits Agency payment card from the project and its implications for 18,000 subpostmasters who own and operate the vast majority of the network of post offices.

1. The Benefits Payment Card

The decision of the previous Government to automate the delivery of benefits payments using the benefits payment card was based on the need to reduce costs, eliminate fraud and ensure beneficiaries would be able to continue to receive their payment in cash from the post office, thus ensuring they retained a choice as to the method of payment which best suited their individual circumstances.

This decision was taken in response to the strong hostile public reaction to a trial which the DSS began in 1993 to test 3 different versions of the pension claim form. Only one version contained a direct reference to payment in cash at a post office, whilst all 3 gave great prominence to payment by ACT. The biased nature of the trial, which could have resulted in the withdrawal of the option to choose to use the post office, appeared to have been undertaken by the DSS without regard to the Government's stated commitment to the nation-wide network. Had the trial been rolled out nationally it would have very quickly threatened the future of at least 5,000 sub post offices.

Government's decision to automate the network promised a far more secure future for all involved with the Counters Business, not only safeguarding the right of customers to choose to receive pensions and benefits from post offices but also

15/08 '99 TUE 10:44 FAX
15/08 '99 10:11 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

007

007

12/11/1999 12:19

GRO

providing a platform on which to develop new products and services for a wider range of clients. This was recognised to be the only way to ensure the future survival and prosperity of the post office network, and it remains the case now.

The NFSP began to develop concerns about the future of the Horizon project during the latter months of 1997. Since then, press speculation surrounding its future has been continuous creating great uncertainty for the future of subpostmasters' businesses, POCL and its current and prospective clients.

2. Welfare reform and the payment card

On 12 May 1998, Kate Hoey MP addressed delegates at the NFSP Annual Conference on behalf of the Minister for Welfare Reform. That speech focused on the Benefit Payment Card, fraud reduction and welfare reform, emphasising the links between them.

Wider access to banking facilities and financial advice for low income groups was stated to be a key aspect of Government's welfare reforms with the aim being for everyone to have access to a basic bank account by 2020. The ability of the nationwide post office network to play a significant role in providing that access and continuing to provide a method of paying benefits was welcomed by the Minister for Welfare Reform.

Post offices have been, and remain, the cornerstone of benefit delivery for the vast majority of people who rely on benefits. The NFSP understands the need to provide a modern, secure payment system which is cost effective, robust and fully accounted.

In the address to Conference, the Minister for Welfare Reform recognised that our partnership with the DSS was crucial in making these objectives achievable for benefits payments through post offices - and that the payment card was designed to do all these things.

15/06 '99 TUE 10:45 FAX
15/06 '98 10:12 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

0008

0008

PAGE 84

NFSP

12/05/1999 12:19

GRO

The business case to warrant the investment being made in establishing a nation wide network through which customers may receive their benefits using the new benefits payment card was based on being only in post offices. POCL is obliged to operate the largest UK retail network, reaching into practically every community throughout the country. Without exclusivity, its ability to provide the service on a commercially sustainable basis was not possible. We therefore welcomed and were reassured by the written confirmation later given by the Minister for Welfare Reform that there were no plans to extend the use of the payment card to other outlets.

3. Government Review of the Project

The NFSP understands that the reasons for the delays experienced by the project were in part caused by the sheer size of the project (the programme was the largest IT project in Europe) and the physical diversity of the post office network. A project of this size and complexity was always likely to have its problems. However, following the award of the PFI contract to ICL Pathway, progress was hampered by the failure of all the parties to agree the detailed project specification. Lack of progress and rising costs led to a major review by Government to decide the best route forward.

Since it became apparent early last year that Government were reviewing its future the Horizon project has been overshadowed. The NFSP remained in close contact with POCL and ICL Pathway during the course of the review, spending a great deal of time dealing with the uncertainty. Our concerns have been constantly relayed to Government and POCL to ensure the decision makers are in no doubt as to the importance of automation to the future of the network.

Confirmation has now been finally received that the payment card will not go ahead because magnetic strip technology is out of date.

15/08 '99 TUE 10:45 FAX
15/08 '99 10:12 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

0009

0009

PAGE 85

GRO

NFS

12/11/1999 12:19

4. Programme Delivery

The system has already been installed in over 250 post offices in the South West and North East of England with all services fully automated. The Payment Card has worked successfully since October 1996 and has been well received by customers, being easy to understand and use.

The work being done at offices has in many cases been significant and is a reflection of the inevitable difficulties of automating a large diverse network.

On the systems side, our understanding is that the system had been moved successfully through the final stages of testing prior to addition of the remaining offices to make up the balance of 300 taking part in the formal live trial. The training courses, go-live arrangements and support arrangements both at offices and via the helplines were ready to ensure a successful trial prior to national roll out.

This experience has emphasised the need for careful planning and management through any trial period prior to automation being rolled out nationally.

5. Impact of the loss of the Benefits Payment Card

Government has stated that it has found a positive way of moving forward on automation as a result of which for the first time ever post offices will have an up to date automation platform, helping them to provide a better service for their customers. Government has further stated that it intends to move to a more modern and efficient way of paying benefits through the post office network, building on banking technology. It intends to do this by transferring between 2003 to 2005 to a system of paying benefits directly by ACT to bank/building society accounts. Post offices will only be one of a multiple of alternative delivery channels. Customers will only be able to retain the choice to pick up their benefit from the post office if the account they have is accessible through the post office.

15/06 '99 TUE 10:46 FAX
15/06 '99 10:12 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

010

010

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12/06/1999 12:19

GRO

NFSP

We view the headline agreement reached between POCL and ICL Pathway as short term protectionism which will have a disastrous effect once the Benefits Agency enforce automated transfer of benefits direct to a bank/building society account. The effect on the network of post offices we estimate to mean the direct loss of up to 40% of all business currently transacted over post office counters.

If automation is completed by 2001 it will be necessary for POCL to strike commercial deals with all banks and building societies to enable those claimants who are their customers to access their account at the post office.

If this is successfully achieved it will mean that the post office network will just be one of a series of delivery channels alongside bank branches, ATM's, supermarkets, telephone banking etc. It is likely that customers will exercise their right to use all of these channels according to their needs. The impact on customers we will return to.

The adverse impact on post offices will be worsened once ACT is enforced as it is inconceivable that customers will continue to use the post office to pay their bills even if they visit the post office to pick up their benefit. This in turn will have a knock on effect on the turn over of the subpostmaster's associated retail business, it being the synergy between the private/post office business that has enabled so many post offices to remain viable.

Many sub post offices already operate on the edge of viability. In these circumstances, with a loss of work on such a large scale, the local post office will not survive, resulting in a loss to those beneficiaries who want to use post office services, including the elderly, infirm and those without transport, people who now are comfortable with transacting their business in the post office environment.

By moving to compulsory ACT, where each beneficiary will need to have a commercial relationship with their bank many may incur bank charges. Banks are now introducing charges to use their services, for example to access an ATM and use counter services.

15/08 '99 TUE 10:46 FAX
15/08 '99 10:13 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

011

011

PAGE 87

12/08/1999 12:19

GRO

NFSP

Memorising a PIN number and accessing cash at an ATM machine makes people vulnerable. A cost effective and secure method of paying benefits - for who?

The impact on the community of the loss of a post office is well known. The sub post office is at the heart of the community and the vital social role subpostmasters play has been recognised many times by Government.

Every day there is a social role played out by the subpostmaster in every community. Who will fulfil that need when the sub post office is closed?

The NFSP's view is that the decision to scrap the benefit payment card will lead to:

- the loss of subpostmasters' investment in their post office business, in which many have invested their life savings and on which they rely for their income and retirement provision. In many many cases entire families earn their living from their post office.
- the prospect of a significant proportion of the current 40,000 sub post office staff losing their jobs, many of these staff being part time, one of the most vulnerable sections of the workforce.
- 17,500 jobs in POCL being put at risk.
- the loss to the community of their local post office, restricting customer choice.

The NFSP therefore wish to ask for the support of the Trade and Industry Select Committee:-

- In opposing compulsory ACT as the costs, both financial and social, will far outweigh the savings the DSS can make by enforcing ACT.
- to ensure the Benefits Agency do not promote ACT until automation of the post office network is complete and contracts with the banks signed.

15/06 '99 TUE 10:47 FAX

GRO

PUBLIC AFFAIRS

012

15/06 '99 10:13 FAX

→ POST OFFICE

012

PAGE 88

NFSP

12/06/1999 12:19

GRO

- to ensure the Government maximises its use of the network for delivery of its welfare reform and "Modernising Government" aims, which needs to be done in a way which is commercially viable for all parties to the contract.
- to encourage all Government Departments which now use the post office network to remain loyal to POCL during the period in which the proposals to maximise the use of the network for the Government Gateway are developed and implemented.

We look forward to the opportunity to expand further on the points covered in this submission.

12th June, 1999

National Federation of SubPostmasters 22 Windlesham Gardens Shoreham by Sea West Sussex
BN43 5RE Tel: 01273 452 324 e-mail: nfsp@mistral.co.uk

15/08 '99 TUE 10:47 FAX

GRO

PUBLIC AFFAIRS

013

15/08 '88 10:13 FAX

POST OFFICE

013

CMA/CWU

Unions have finally been asked to participate in the future of the project due to an agreement signed on 24 May 1999.

They don't feel that the project had been properly thought through by the last government(having tried to borrow the Irish system)

Q: Reactions of staff to the Swipecard?

A: It was popular with staff. Saved around £2m in fraud.

They would like a commitment from the government that they will open up other schemes.

They feel that some good industrial relations have developed in the last 2 years.

Q: Is the management prepared to back up the implementation of the system with relevant training etc.

A: They are prepared to do anything that is necessary.

Q: What are your views on barcoding?

A: Barcoding is fine except that it is a temporary expedient.

Q: How confident are you that in 5 years time you will have a share of the work?

A: If the govt manage to do what they said there will be an extremely bright future. If they don't manage to do what they have planned there will be some trouble in that it will mean longer hours, protracted work etc.

15/06 '99 TUE 10:48 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

014

014

15/06 '99 10:13 FAX

HP2

CWU/CMA SUBMISSION TO THE TRADE AND INDUSTRY SELECT COMMITTEE ON POST OFFICE COUNTERS AUTOMATION

INTRODUCTION

1. The Communication Workers Union (CWU) represents around 165,000 non-management employees in the Post Office, over 11,000 of whom work in Post Office Counters Ltd (POCL). The Communication Managers Association (CMA) is the representative body of all management grades within the Post Office. We therefore have a great interest in the automation of the Counter's network under the Horizon project, and its implications for the future of POCL and the Post Office as a whole.
2. To date the negotiations around the Horizon Project, and the problems encountered within it, such as the delay in implementation, have been between the contract partners; Post Office Counters Ltd, ICL and the Benefits Agency.
3. This submission is therefore made on the basis of knowledge gained by the Unions through the industrial relations interface with POCL and through our contact with Government, as well as by what has been reported in the press over the last few months. The Unions make these comments, as we believe it is our responsibility to play a part in any discussions that impact upon the future security of the Post Office network as a whole, as this enables us to enhance our members employment security and use our knowledge of the service to ensure the public interest is protected.
4. The new working group announced by the DTI Minister of State Ian McCartney on 28 May 1999 will be our first direct involvement in the project at this level. We hope it will help develop a sensible solution to the problems encountered so far during the development and trial of the Horizon project.

15/08 '99 TUE 10:48 FAX
15/08 '99 10:14 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

015

015

5. We are confident that our knowledge of the industry and our desire to see the success of this project will help in facilitating these discussions alongside the other interested parties, so that a favourable outcome can be realised.

6. With these factors in mind the postal Unions would like to make the following comments regarding certain core problems and issues which we believe the Select Committee may wish to explore concerning the Horizon project:

■ THE REASONS FOR THE DELAY

7. Our view is that for one reason or another either directly or indirectly all parties to the contract may have contributed to the delay.

- The previous Government must share a good deal of responsibility for the delay. In its rush to be seen to be tackling fraud the Conservative administration was happy to initiate the launch of a system without fully understanding both the technological capability of the system and the cost involved to both the Post Office and Government Agencies.
- ICL appears to have had problems with the technology it developed. We understand that the magnetic swipe card system it has attempted to introduce was modelled on the one used by the Irish Post Office (An Post) which works well, and is an efficient way of paying benefits and reducing benefit fraud. However, we gather that there have been major problems in transferring this type of system to a much bigger network and "scaling up" the technology for the UK.
- The Benefits Agency (BA) has for a long period wished to provide benefits by means of Automatic Credit Transfer (ACT). This remains its long-term objective. In order to meet the needs of the Horizon project its existing technology would need to be compatible with the magnetic card or smart card planned for use under the project. We understand that to date this has not happened. It is impossible for us to say why this delay was caused, but the desire to move away from Horizon and on to the ACT system would no doubt have influenced its judgement.

15/06 '99 TUE 10:48 FAX
15/06 '99 10:14 FAX

GRO

PUBLIC AFFAIRS

POST OFFICE

016

016

- Post Office Counters Ltd (POCL) has been keen to ensure that any new technology is not only suitable for the purpose it was originally designed for, but that it will be compatible with its future business vision. In particular POCL needs to be confident that it will have the ability to adapt such technology to be fit for purpose, specifically to fit its vision of POCL as a network bank. It has acknowledged the role that Horizon would play in performing its current business in a better and more efficient way. In practice this has meant developing technology to execute the transition from paper-based order books to the new screen technology. POCL's objective has been to ensure that it has 100% confidence in the system before it is rolled out. Thus it is far better to encounter some delay in order to be certain that the system fits not only current services but can be adapted, by the use of software modules, to perform new business in the future.

• ASSESMENT OF SWIPE CARD TECHNOLOGY

8. The principle benefit of the magnetic swipe card, or the future use of smart card technology, is that it would be better at preventing fraud than the bar-coding of order books that will now be in operation instead. We understand that this was verified by the trials carried out by POCL. The Post Office clearly shares an immediate interest in curing benefit fraud and introducing this technology as it is obliged to compensate the Benefits Agency for a proportion of the amount defrauded.
9. The smart card would also have the additional advantage of enabling customers to access further electronic Government services through the post office network. These services could range from accessing information to the provision of on-line healthcare.

• ROLE OF THE BENEFITS AGENCY

10. We understand that the Benefits Agency (BA) failed to prepare itself and its systems sufficiently in order to be compatible with Horizon. However, without having had a role in the negotiations, it is impossible for us to say whether this was a deliberate action in order to facilitate the demise of Horizon and lead to the introduction of ACT as their preferred option.

15/06 '99 TUE 10:49 FAX
15/06 '99- 10:14 FAX

GRO

PUBLIC AFFAIRS

POST OFFICE

0017

0017

11. It is possible that the reported failure of the BA to complete the necessary work on its system was due to technological problems, or alternatively a result of difficulties between the various stakeholders. In a project of this size and importance with such wide-ranging implications, it is almost inevitable that some conflicts of interest will arise. It may be a deficiency of the way in which the Private Finance Initiative (PFI) operates but, at any stage in the development, design or trial of a project, there can be delays if all those directly involved are not totally committed to moving in the same direction at the same time.

• CONTENT, TIMESCALE AND FINANCING OF HORIZON

12. As the Unions have been outside the negotiations on Horizon, we do not have a full understanding of the implications of the variation in the contract between the stakeholders and the knock-on effects. In particular, we have not been party to detailed information on the financing of the project, and look forward to meeting with working group representatives and especially with POCL to discuss the implications of this and the potential loss of income involved.
13. We do understand that time and money has been lost while we wait for this project to be rolled out, and that the delay is not good for anyone concerned. Aside from the advantages of cutting benefit fraud, a fully automated and on-line post office network would be a much more attractive partner to develop access to Government services, or even for organisations wishing to bid for the National Lottery contract in future.

• SIGNIFICANCE OF GOVERNMENT ANNOUNCEMENT

14. The Government's announcement represents a welcome move and was significant in that it provides a vehicle for the continuation of the Horizon project. It appears that the project had reached the stage where the only alternative was termination, which would be the worst scenario for our members and our members' jobs, as well as the public who would be faced with a large-scale reduction in the Post Office Network in general. If the Government really wants to prevent

15/06 '99 TUE 10:50 FAX

GRO

PUBLIC AFFAIRS

POST OFFICE

0018

0018

15/06 '99 10:15 FAX

fraud and move forward in developing a successful, modern and expanding Post Office in the future, it cannot afford to cancel Horizon.

MOVING FORWARD

15. This submission is an attempt to provide the Select Committee with an outline of the situation regarding Horizon as we understand it. As we have mentioned several times during this submission, we have not been party to the negotiations so far.
16. However, we hope and believe that the establishment of the working group announced by the DTI Minister of State on 28 May 1999 will allow us to draw on our knowledge and understanding of the industry and participate directly in developing solutions to the problems encountered by Horizon. We look forward to working with all the interested parties, and believe that such a working group is long overdue. Provided that all parties are committed to the success of this project we believe that an outcome favourable to all concerned can be reached.

14 JUNE 1999

RD99/164/1

15/06 '99 TUE 10:50 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

019

019

15/06 '99 10:15 FAX

ICL

Q: The programme is three years late. What is the problem? Managed to implement the lottery within 12 months, why the delay this time?

A: The payment card has been running successfully since September 1996. They feel that there is more work than they had originally felt and this has taken time to sort out. This is one of the things that they have looked at in their latest review.

One of the problems has been one contract for two companies. It is very unusual for ICL to enter into such a contract especially with such a large customer.

Q: The POCL has been very keen but the BA not so keen. Is that a fair conclusion?

A: That is not the conclusion that they would draw.

Q: Have ICL received the same amount of help from the same parties?

A: The BA couldn't provide certain information in Sept 96 although it has trickled through since then.

They have since had to meet and re-plan the contract so that the two of them could meet their conclusions.

Q: Is that right that you had to get the BA to agree in writing to meet their side of the contract? Isn't that very odd?

A: It is not that odd seeing that the contract demanded good connection between the two parties. The contract relied on very close interdependency and that is why a written agreement was called for.

Q:BL: What has gone wrong? The technology is there and has been implemented by ICL previously (Lottery) but this time it is has not worked out. Why?

A: It is one of the most technically demanding jobs that ICL have ever undertaken.

Q: Fair to say that it is one hell of a mess?

A: The quality and quantity of the work undertaken has been of the highest they've known. ICL have taken out £180m against this scheme to cover any loss.

15/06 '99 TUE 10:50 FAX

GRO

PUBLIC AFFAIRS

POST OFFICE

020

020

15/08 '99 10:15 FAX

Q: BL: Was the project just too large and too ambitious? Can it be delivered?

A: The task is manageable. Although, ICL have learnt the lesson from this venture that a contract of this size really needs one customer and one provider. When you introduce more than one customer you enter into greater complexities

The PDA (programme Development Authority) started off with the right intentions. It then had to go back and renegotiate the contract with the two customers.

The PDA agreed at the end of their first review at the end of 1997 that the POCL were the main client of the contract.

Q: The govt are saying that the card is outdated. Would you agree?

No. They have worked well while they have been in use.

ICL suggested to the BA in 1995 that it may be better to start with a smartcard as opposed to a magnetic swipe card. However, the BA decided that they wanted a swipe card as opposed to smartcard.

The magnetic swipe card is a well-used system around the world but the smartcard offers greater uses

Q: On the contract with PO that is to run until 2005.

A: ICL have revised their contract with the PO and have removed all refs to the BA. They have changed the contract so that they receive payment for the infrastructure of the system as opposed to a payment for each transaction. The current contract sees ICL losing £100m as opposed to being in profit as for the previous contract.

Q: Is the card a payment card for the PO or an all-round cash card?

A: It offers the concept of a universal bank – all facilities can be carried out through the PO. This is an achievable goal for the PO. They visit all Post Offices and survey them. The equipment in place in 300 Post Offices will remain there after testing.

They had to look at the amount of services that the PO offers. 170 products are provided. They have learnt from this and also from the size of the PO itself – having to train 70,000 Post Office masters etc.

They have also noted how committed most Post Office masters are at getting automation in place.

15/06 '99 TUE 10:51 FAX

GRO

PUBLIC AFFAIRS

021

15/06 '99 10:15 FAX

POST OFFICE

021

Q: Why have they not considered legal action against the BA?

A: It won't happen. They have renegotiated their contract.

Q: Would you enter into other contracts of this (PFI) nature again?

A: ICL already are entering into other contracts of this nature.

ICL have tried to make the system as easy to use as Post Office possible. It is web friendly from the beginning and the hope is that it will have the technology for people to use it through their TV and kiosks etc.

The PO is in a better Position than any other group to cope with the demands of electronic delivery of govt services.

15/06 '99 TUE 10:51 FAX

GRO

PUBLIC AFFAIRS

15/06 '99 10:15 FAX

POST OFFICE

022

022

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ICL PATHWAYSUBMISSION TO THE TRADE AND INDUSTRY SELECT COMMITTEEHistory - 1996

1. In May 1996 ICL Pathway won the tender to computerise all the UK's 19,000 Post Offices and simultaneously automate the system for paying DSS benefits to a total of 28 million claimants. This was a Private Finance Initiative (PFI) project under which ICL Pathway would design, build, finance and operate the system, taking on all the initial risks and being rewarded by receiving a fee for each transaction conducted over the new system. The contract was to run until 2005; the customers were the DSS Benefits Agency (BA) and Post Office Counters Ltd (POCL). Contract details were due to be completed by the end of 1996 and national installation in all post offices was to be completed by the end of 1998.
2. ICL Pathway (initially the Pathway consortium, since 1996 a wholly owned subsidiary of ICL) had been formed in 1994 to bid for the tender. It was selected following a lengthy competitive bid; its subcontractors include Girobank and De La Rue.
3. One of the largest IT projects in Europe, the proposed network is twice as large as all of the current banking infrastructure in the UK. The project would also involve ICL Pathway training 70,000 post office staff, and designing and integrating the system to handle some 20 DSS benefits paid to a total of 28 million claimants (many of whom receive more than one benefit) at post office counters. Since billions of pounds are paid out every year, the system had to be extremely robust and secure.
4. The new system, when fully installed, would enable POCL to offer more services to their current and prospective customers. A major attraction of the system was its capability virtually to eliminate fraudulent DSS benefit encashment, resulting in estimated fraud savings of £150 million a year.
5. As specified by the two customers in the contract, ICL Pathway would deliver a magnetic stripe swipe card (the Payment Card) which would gradually replace order books and girocheques. ICL's original proposal was to issue a smartcard but the customers maintained their preference for a "mag stripe" Payment Card. Currently some 890 million order book and girocheque payments are made through post offices each year.
6. In May 1996 the customers established the PDA (Programme Delivery Authority) to oversee the project, the PDA's 150-strong staff being formed from POCL, BA and external consultants. In September 1996 the first ten post offices in the Stroud vicinity were automated with the new system and the first benefit Payments Cards were issued for claimants to receive Child Benefit only.
7. The ICL Pathway system was dependent on information received from the systems of both customers, ie this was an end-to-end system where DSS systems would

15/06 '99 TUE 10:52 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

023

023

15/08 '99 10:18 FAX

transmit data through the ICL Pathway network to the relevant post office (and vice versa).

8. The original contract timetable was based on the agreement that the BA would make its CAPS database (Customer Accounting and Payment Strategy) available to ICL for testing in September 1996. This software and the interface specifications were essential to ICL Pathway, to enable the establishment of the databases for all benefits so that the ICL Pathway system could pay the right money to claimants at the right post office at the right time. CAPS is run in-house by the BA. However, it subsequently emerged that it would be available only on a phased basis and would be delayed by three years. Today, as ICL understands it, it is still not fully completed.

1997

9. In June 1997 the system in the first ten post offices was upgraded to introduce bar-coding of order books. (In an earlier contract signed in 1994 ICL had introduced bar-coding on order books presented at all post offices within the M25 area, which still runs successfully and which has led to tangible savings in encashment fraud through the impounding of fraudulent order books).

10. However, in the course of 1997 it gradually became evident to ICL Pathway that the project was being managed by the PDA in a manner inconsistent with the principles of a PFI as explained in guidance issued to departments by HM Treasury and the Treasury PFI Taskforce. Although as a PFI contract a significant amount of risk was being laid on ICL Pathway, the PDA maintained it had a right to require ICL Pathway to behave as if this was a conventional government procurement programme. This led to a huge amount of senior management time being devoted to solving the issues which were constantly being raised by the PDA. Accordingly, ICL, POCL and BA sponsored an independent report from PA Consulting. This concluded its Review in October 1997 and one important result of this was the abolition of the 150-strong PDA. But a significant amount of time had been lost.

11. In November 1997 the ICL Pathway system was extended to a further 200 post offices in the north-east and south-west using the benefit Payment Card to pay Child Benefit. The technology was acknowledged as working successfully and was well received by sub-postmasters, their staff and claimants alike. At the same time, the BA claimed that ICL Pathway was late in delivering under the terms of its contract. This is not the case: a revised timescale and programme had been agreed by all parties including the BA, and ICL Pathway was delivering to schedule.

1998

12. In early 1998, because of what it regarded as excessive interference and bureaucracy, ICL approached HM Treasury to register its concern. As a result, the Treasury Expert Panel under Adrian Montague of the PFI Taskforce was established to assess the commercial and technical feasibility of the project. This Panel reported its findings in July 1998, which confirmed the technical viability of the project and the approach of ICL Pathway. It was then indicated to ICL that relevant Ministers would meet to consider the way ahead, but the Cabinet re-shuffle at the end of July prevented this taking place.

15/06 '99 TUE 10:53 FAX
15/06 '99 10:16 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

024

024

13. In September 1998 Graham Corbett, deputy chairman of the Monopolies and Mergers Commission, was appointed by the Government as 'facilitator' to determine a way forward to meet the needs of all parties to the contract (ICL Pathway, POCL, BA). He concluded his discussions with the parties four weeks later. From October to December 1998 ICL Pathway held detailed negotiations with BA and POCL, making a number of revised proposals which represented serious concessions, in order to gain acceptance on a commercial way forward. On 18 December ICL Pathway submitted its final proposals which were to be presented to Ministers, who were expected to meet shortly thereafter to reach a decision. However, Ministerial resignations before Christmas and another, subsequent reshuffle prevented this taking place. ICL has not, in fact, ever received a reply to its letter of 18 December 1998 and in April 1999 formally withdrew this proposal.

14. By this time some 36,000 claimants were successfully using the new benefit Payment Card at 204 post offices to collect Child Benefit. Even on this relatively modest basis, the system including the electronic scanning arrangements for order books generated £2 million in potential fraud savings. Throughout this period of almost constant review since February 1998, ICL Pathway continued to work on the project at a cost of £10 million per month.

1999

15. In January 1999 it emerged that the BA did not wish to proceed with the magnetic stripe card, preferring instead to make direct payments into bank accounts – notwithstanding the fact that many millions of legitimate benefit claimants do not have bank accounts and, because they rely on their benefits, are unlikely to be able to open bank accounts. ICL Pathway was, however, not informed whether Ministers collectively had decided to dispense with the Payment Card.

16. In late January a senior Treasury official, Steve Robson, was appointed with the Prime Minister's authority to devise an alternative solution. ICL Pathway fully co-operated with him. His proposed solution was to preserve the Post Office infrastructure and eliminate the magnetic stripe card, paving the way for the possible introduction of a smartcard and a simple banking role for POCL. Benefit claimants would use their smartcard to access their benefit account at the post office and the BA would pay the benefits direct to these accounts or to an account in a conventional bank if the claimant wished. It is worth noting that although ICL Pathway had developed a magnetic stripe card as stipulated in the 1996 contract, ICL Pathway designed the system to be capable of using smartcards from day one.

17. From February to May 1999 ICL Pathway made strenuous efforts to achieve a solution acceptable to all parties, but by May it was clear that Ministers had decided not to proceed with the Payment Card. On 24 May the Government through the DTI announced the revised agreement for a partnership between the Post Office and ICL to deliver the new infrastructure but without the BA Payment Card or a smartcard. In the meantime, a further 100 post offices had been equipped in the run-up to national installation of the system across the UK.

15/06 '99 TUE 10:54 FAX

GRO

PUBLIC AFFAIRS

025

15/06 '99 10:17 FAX

POST OFFICE

025

Project Achievements

18. This submission seeks to make it clear that, in addition to the measurable savings in benefit encashment fraud cited above,
- ICL Pathway has delivered a working system since 1996 that has been subject to rigorous external reviews, each of which has validated its technical feasibility.
 - ICL Pathway has designed a system that would have enabled the BA fully to reconcile its accounts (this element of the system is successfully in place for the payment of Child Benefit at the operational post offices).
 - ICL Pathway has gone to very considerable lengths throughout the duration of the project to date to find an acceptable commercial way forward; the issue has not been the technology.

The Future

19. Following the policy change within the DSS to discontinue the use of the benefit Payment Card, the three parties to the original contract have agreed a revised programme as follows:
1. The original PFI contract with ICL Pathway has been revised so that payment will no longer be linked to transaction volumes, reflecting the removal of the Payment Card element.
 2. ICL will have a single customer, the Post Office.
 3. The fixed price contract for ICL will run until March 2005.
 4. ICL and the Post Office will continue discussions on a Public/Private Partnership for the development of Network Banking and 'Modernising Government' services which may be built upon the Pathway platform.
 5. The electronic scanning of benefit payment order books will be implemented on a national basis, and will contribute to reducing benefit encashment fraud.
 6. ICL will complete automation of all 19,000 post offices and installation of the IT network. By January 2000, automation will be running at a rate of 300 post offices per week, with the programme scheduled for completion by April 2001.
20. As a consequence of this, in line with accountancy requirements ICL has made a provision for £180 million in its accounts for 1998/1999, representing the cost of its investment in the Payment Card to date. The deadline for signing the revised agreement is 16 July 1999.

ICL

11 June 1999

15/06 '99 TUE 10:54 FAX

GRO

PUBLIC AFFAIRS

15/06 '99 10:17 FAX

→ POST OFFICE

026

026

POST OFFICE

Q: Not so happy with ICL now? What happened?

A: After the Treasury review it became clear that there was a change in policy at the DSS. They wanted to pursue an alternative option.

PO felt that they had had it tied down by Christmas. One of the problems was that the DSS is a key customer of the PO so they had to try and accommodate the position taken by the BA.

PO has seen the automation programme as essential to the survival of the PO network.

The Mod Gov White Paper said that the Post Office would be equipped with the ability to provide electronic government.

Q: What are the advantages of the PO having the payment card?

A: The PO can offer the human face of automation. The PO will act as the interface between transactions.

SS: It's clear from market research that although 70% of benefit receivers have bank accounts they prefer to collect their benefits in cash from the PO.

Q: What about the 30% that don't have bank accounts?

A: PO hopes that the govt offers them the choice. PO must facilitate the choice that the user wants. PO would like to provide both options not dictate which options the user must have.

One third of PO revenue comes from DSS - important customer.

Q: RB: The Govt should do what?

A: The government should move toward ACT as the best option. The issue is how that is done and how quickly.

The PO would like to see it in place because it would then draw customers into Post Offices who would then buy other things (stamps etc.)

They would like to ensure that the govt doesn't withdraw other govt services provided through Post Offices

They would also like to ensure that the PO operates on a level playing field.

15/06 '99 TUE 10:55 FAX

GRO

PUBLIC AFFAIRS

15/06 '98 10:17 FAX

→ POST OFFICE

027

027

The concern that banks are just waiting for the system to opened up is not borne out by the fact that a lot of banks greet the prospect with something less than enthusiasm.

There were reasons why a swipe card was a better option three years ago but the development of technology in that time has meant that perhaps, with the benefit of hindsight, it was a poor idea. They should have opted for the smartcard from the off. Now, they can implement the smartcard and they accept that the smartcard is the way forward. All equipment will be smart card friendly.

The change of funding from PFI to customer based funding throws the emphasis back onto the PO.

Q: AM: Is it fair to say that the PO would not entertain a PFI deal again with three parties because the two customers had different agendas?

A: To a certain extent. Don't want to apportion blame but should see the progress made in the last 12 months.

Most of the cost has been borne by ICL because initial outlay has been on technology.

Q: BL: How is barcoding going to help PO or is it virtually obsolete now?

A: Barcoding will help detect fraud or a book that should be withdrawn provided the system stays the same.

The PO held a review at the beginning of 1998 and three objectives emerged:

- 1) They wanted to stay in the cash market
- 2) Government Gateway - they wanted to be a provider of personally automated government services
- 3) Wanted to continue providing services for Royal Mail and Parcelforce

15/06 '99 TUE 10:55 FAX
15/06 '99 10:17 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

028

028

HP 1

Memorandum to Select Committee Trade and Industry
Horizon Project

Background

- 1 POCL has developed a Mission and Vision which outlines a business strategy for the next 10 years, building on the key strengths of its unrivalled reach, its infrastructure, and its trusted brand.
- 2 The POCL Mission is to become the UK's number one choice for the important business of everyday life. This will be achieved by concentrating on four key markets in which it has real competitive advantages.
- 3 POCL aims to be the UK's most trusted and used:
 - access point for official information and transactions
 - wholesale cash distributor
 - access point for cash deposits and withdrawals on behalf of many banks
 - provider of transactions and specialist advice on all aspects of Post Office mail and distribution activities.
- 4 Providing a highly competitive infrastructure which connects post offices to each other and to others' systems in a secure and efficient way is key to our success in these markets.
- 5 The Horizon project is a cornerstone for this and it builds a platform on which services can be developed. The platform will also be designed to enable other technologies to be connected to it and the equipment is able to handle smartcards, magnetic swipe cards and barcodes.
- 6 The benefit payment card was seen as an important step strategically to retaining customers and migrating them onto a Post Office Smartcard, which would be able to do many things including providing electronic access to Government services.
- 7 It would also provide significant fraud savings to the Benefits Agency, as well as proper reconciliation of its accounts. Benefit recipients like to be able to collect benefits from post offices and 77% said the benefit payment card was as good as, if not better than, the order book.

Horizon Programme - Pre contract

- 8 The origins of the Horizon programme can be traced back to circa 1992. Previously, customers had always had equally positioned choice as to how they wished to receive benefit or pension payment, either through post offices or bank accounts (via ACT). In late 1992, DSS began a trial of a new benefit entitlement claim form which omitted use of post offices. Following extensive campaigning by the National Federation of Sub-Postmasters (NFSP) to the

15/06 '99 TUE 10:58 FAX

GRO

PUBLIC AFFAIRS

029

15/06 '99 10:13 FAX

POST OFFICE

029

effect that the trial represented a threat to the viability of post offices, the claim forms were withdrawn.

9 Ministers asked senior management from POCL and senior civil servants from the Department of Social Security to undertake an end to end review of the product design and come up with something that addressed the three main drawbacks of paper based methods of payment, namely cost, fraud liability and lack of customer level accounting information.

10 The BA/ POCL Joint Feasibility study examined 3 main options (along with several variants); use of barcodes, use of a magnetic swipe card, use of a smartcard. The report concluded that a magnetic swipe card offered the most effective (as well as cost effective) way forward. This approach was endorsed by ministers.

Procurement and Contract

11 A joint programme known as 'Bringing Technology to Post Offices and Benefit Payments' was established, led by a senior DSS civil servant and consisting of staff from BA and POCL, supported by specialist external consultants where needed. The programme followed a procurement process in line with Government and European regulations.

12 Contracts were signed between BA, POCL and ICL Pathway and between BA and POCL on 15 May 1996. Contracts between Social Security Agency Northern Ireland (SSA) and POCL were signed in June 1996. The programme moved from procurement into delivery phase and was renamed the Programme Delivery Authority. The contracts signed envisaged that all outstanding issues would be resolved and that software and the solution would be ready for model office testing in January 1997, to be followed by a live Operational Trial beginning in April 1997, with full roll out commencing in July 1997, and completing by the end of 1998.

13 In line with PFI methodology of allowing the contractor to develop a solution to meet business requirements, the signed contracts contained hundreds of requirements and associated solutions which were expected to be extrapolated into detailed schedules of service descriptions. This process took eight months rather than the three originally allowed.

14 An early version of the benefit payment card solution was developed and went live in one post office in September 1996 followed by a further nine post offices in October 1996.

15 Slow progress resulted in a re-plan in December 1996. The Operational Trial was rescheduled to take place from August 1997 to November 1997. This re-plan was carried out through the agreed change control process and signed by all parties.

15/06 '99 TUE 10:57 FAX

GRO

PUBLIC AFFAIRS

→ POST OFFICE

030

030

15/08 '89 10:18 FAX

16 The programme continued to make slow progress and to protect the Authorities' (ie BA and POCL) contractual position, as completion of the Operational Trial had not been achieved by November 1997, a notice of default letter was sent to ICL Pathway. ICL Pathway rejected the letter and have since claimed that the Authorities impeded their ability to deliver the trial and that the dates do not hold.

17 The programme has been reviewed several times, by POCL and BA internal auditors and external consultants. In particular, PA Consulting performed a strategic review of the programme in September 1997 on behalf of DSS, POCL and ICL. It concluded the programme was technically feasible, that it would take longer and cost more to deliver, was of a complexity underestimated by ICL, and that there was no sensible way of descoping/ radically altering the plan. Overall it was better to continue than to terminate.

18 In December 1997 ICL requested new commercial terms to compensate them for the delays to the project. The Authorities rejected their claims. However ICL kept pressing for new terms with further discussion papers and began lobbying to further their case.

19 POCL took over line management of the programme (renamed Horizon) in April 1998, as recommended in the PA Consulting strategic review.

20 In June 1998, against a background of concern about delay to the project and its ability to deliver its objectives, HM Treasury (HMT) commissioned an independent review of the programme and asked a panel of experts to make recommendations, published in July 1998. These were broadly in line with previous reviews, finding the programme technically viable though complex, and that there was likely to be further delay and cost implications for each party's business case.

21 Ministers considered the report along with other submissions from a working party chaired by HMT on the future of the programme. Three main options emerged: continue with the benefit payment card (BPC), continue without the BPC or terminate the programme. Ministers asked if a way forward could be found between the three parties.

22 In September 1998 Graham Corbett, Deputy Chairman of the Monopolies and Mergers Commission, as an independent adviser was appointed by HMT to facilitate discussions between the three parties on an acceptable way forward. He recommended:

- contracts between POCL and ICL Pathway would be extended to 2010,
- contracts between BA and POCL, and BA and ICL Pathway extended to 2008.

15/06 '99 TUE 10:58 FAX

GRO

PUBLIC AFFAIRS

15/06 '99 10:18 FAX

- POST OFFICE

0031

0031

- POCL also agreed to pick up the costs of replacing the basic infrastructure equipment in 2006 and the additional costs of PIN pads to facilitate a banking service in line with the vision.

ICL and The Post Office were asked to work up a Public/ Private Partnership Heads of Agreement as a possible way forward. This was duly done and provided ICL with a way to make further concessions towards the public sector position and allowed them to accept a loss on their business case.

23 ICL made a final offer on 9 December 1998 and The Post Office agreed to bridge the gap by picking up increased prices to ensure continuation of the programme and the BPC. ICL still, however, were required to accept a loss on their business case. This deal would have provided POCL with a more certain route to Network banking and the terms were additionally offset by a large reduction in residual risks held by POCL.

1999

24 During 1999 a series of different options were tabled by Government, culminating in a proposal which removed the BPC but rolled out the remaining infrastructure. In the meantime POCL would be expected to develop new banking relationships with compulsory ACT being introduced in 2003. This Horizon system would also provide interim (but not complete) fraud savings by reading the barcodes printed on order books.

25 This became the preferred Government option which Ministers wished to have implemented. Negotiations then took place between Government and ICL on the cost of the new contract and in the light of these The Post Office signed heads of agreement on the basis of which we are now attempting to negotiate a full agreement by the end of July.

The Post Office
11 June 1999