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WITHOUT PREJUDICE - SUBJECT TO CONTRACT
COMMERCIAL IN CONFIDENCE

BA/POCL AUTOMATION: FINAL REPORT TO MINISTERS APRIL 1999

Conclusion

- Treasury officials are strongly of the view that termination of the contract with ICL in order to pursue an alternative solution offers the only way forward. It offers a clean break; it simplifies the commercial relationship between POCL and ICL should they find something to salvage (if that is a sensible and affordable way forward); it removes BA from the contract and - in the face of likely further delays and difficulties with delivering option A - it offers better value for money. There will be some very difficult presentational issues to be tackled, but HMT/DSS believe these are manageable;

- Trying to revert to Option A is not viable. Treasury officials judge that relationships within the project are now too dysfunctional to give Ministers any comfort that the project will be delivered. Furthermore it is unclear that ICL will be prepared to continue with the project on this basis;

- The considerable additional cost of option B cannot be justified. Additional revenues from option B to offset the costs (to the extent that they materialise) could similarly be realised from pursuing alternative options. Treasury officials therefore recommend that this option is rejected. This view is strongly reinforced by POCL's unwillingness to bear any of the funding gap for Option B on the strength of the potential future revenue streams, and their apparent preference for termination over Option B1;

- under all options, there is a clear need to properly incentivise POCL and its management to reduce network cost, sharpen their business strategy and aggressively pursue new business. A radical reform is required.

History

The BenefitsAgency/Post Office Counters Ltd automation project (known as the "Horizon" project) has a long and troubled history. It was initiated in 1993 with the following objectives:

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- to provide a more secure and efficient way of paying benefits. Benefits would be authorised by a magnetic strip card (the "benefit payment card", BPC) rather than via the current paper-based system. The aims were to eliminate encashment fraud (costing over £100m a year); to provide DSS/BA with the means to account fully for their programme expenditure; and to reduce administration costs (but only marginally).

- to modernise and automate PO Counters to make their current (paper-based) business more efficient, and to help them win new business.

- to provide a secure revenue stream from POCL's biggest customer (both via direct income from BA and footfall income from other transactions with benefit customers) into the next decade.

- the prospects of an automated platform has also enabled POCL to begin to develop a commercial vision for the period when income from BA reduced. This is to provide "network banking" services as an agent for the major high street banks; and to develop a "citizen smartcard" providing electronic interaction between the public and government.

2. A private finance contract was let to ICL Pathway after a competitive tender in May 1996, with a view to complete roll out by October 1998.

<u>Why is Horizon under review?</u>

3. It soon became clear that the complexity of the project had been underestimated and there was a final replan of the project in February 1997. However further delays ensued, and in November 1997 ICL Pathway was placed formally in breach of contract by both POCL and BA after a key contractual milestone was missed. BA subsequently issued a legal "cure" notice, which (in the view of their lawyers) allows them to take steps to terminate their contracts with ICL Pathway.

4. The project is now running three years behind schedule. New deadlines have been set at various times and consistently missed by ICL. BA and POCL attribute the cause of the delays to ICL in all material respects and this has been endorsed by external reviews (including a very recent confidential report which has concluded that the fundamental cause of problems is that ICL have failed throughout the process to analyse and then address POCL and BA's detailed requirements). Pathway has responded by blaming the public sector for the

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delays and has sought extensions of the contract and price increases to recoup its costs.

5. A number of detailed technical and policy reviews have been carried out by officials to find a way forward. Following a technical report by independent experts in July 1998, which showed that the Horizon infrastructure was viable and "future proof", the public sector parties began negotiating with ICL Pathway to reach an acceptable commercial deal. At the same time officials from DSS, HMT, DTI, BA and POCL reviewed contingency options.

6. Following the failure of negotiations (the so-called Corbett discussions) to establish a commercial basis acceptable to Government for proceeding with the contract in October 1998, ICL were given further time-limited periods to move further towards the public sector's position and to make progress in their discussions with the Post Office to develop a public/private partnership, as a means of enabling ICL to bear a larger loss.

7. ICL wrote to the Chief Secretary on 9 December (and again on 18 December to make a number of further small concessions) with their "last and final" offer. This moved further towards the public sector's position in NPV terms (including taking on more risk) and offered the required Fujitsu guarantees on funding. The offer involved ICL taking on an expected loss on the BPC project of £126 million in net present value (NPV) terms. ICL's acceptance testing proposals (agreed with the Post Office) were still unacceptable to DSS/BA (in the light of recent experience with NIRS 2, Alistair Darling is seeking further reassurances to safeguard the delivery of benefits). In the areas of both risk and acceptance testing, the ICL proposals represent a reduction against the terms agreed in the original contracts. The Post Office Chairman wrote to the (then) Secretary of State for Trade and Industry stating that the PO Board endorsed the deal and would bridge the remaining gap between ICL and the public sector from their resources. A number of other commercial and contractual issues remain unresolved.

8. However, Ministers were still unhappy with ICL's offer. Given ICL's failure to deliver, they sought a solution which might be better matched to meet Government's wider objectives. After an initial set of discussions between Steve Robson (HMT) and ICL, the Prime Minister agreed (Jeremy Heywood's letter of 1 March) that the public sector parties - under Steve Robson's chairmanship - should take forward negotiations with ICL on an alternative option which would allow BA to move to payment of benefit by ACT whilst

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retaining footfall in Post Offices, and would retain ICL in the partnership.

9. This report sets out the three options now available to take the project forward:

- Option A: accept ICL's offer of 9/18 December (subject to resolution of acceptance testing) and continue with the project, including the benefit payment card;

- Option B1: indicate to ICL and POCL that the alternative solution which removes the benefit payment card is acceptable, subject to final agreement to contractual details;

- Option 3: terminate the contract with ICL and pursue an alternative solution involving the payment of benefits into conventional bank accounts across PO counters.

We have considered the value for money of each option for the public sector as a whole. The results of KPMG's modelling of the NPV impact on the public sector for each option is at Annex A.

Should we revert to Option A (Benefit Payment Card)?

10. Taken at face value the figures suggest that Option A remains the best value for money option in NPV terms. But the figures assume it is delivered to the cost and timescale set in December. Deliverability in practice heavily depends on whether Option A is still a realistic option, in terms of whether it could be implemented against the background of the current client-supplier relationship involving three parties - BA, POCL and ICL; and the failures to date on the part of ICL.

11. On technical viability, as noted above, the report of the independent panel last summer concluded that Option A is technically viable and "future proof", and should be successfully delivered, *assuming firm management of the project and commitment and goodwill on all sides*. That is probably still the case now (although DSS/BA would disagree). But since the report there have been further problems with testing and plans have slipped. ICL have already missed the first milestone in the timetable agreed in the course of the Corbett negotiations; and BA point to faults that emerged in the latest testing of the Model Office as an indication of further delays of at least six months: and the

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roll out will now cut across the sensitive Millenium period. For their part, ICL have expressed concern at what they see as delays to the multi-benefits element of BA's CAPS system, which is an essential part of the successful implementation of Option A - although BA/DSS say this is totally unfounded.

12. The impact of a further delay on the NPV of the project has been modelled. BA estimate (although ICL and POCL do not agree) that the latest difficulties could delay roll out by a further 6-7 months. This would worsen the NPV of option A significantly - by £110m NPV. DSS/BA argue that the NPV could worsen further once acceptance testing is resolved to their satisfaction.

13. Treasury officials are principally concerned about the relationship between the parties. The Benefit Payment Card project was always a compromise between the objectives of BA and POCL. As currently formulated, it offers considerably more to POCL than it does to BA:

- for POCL it locks in revenue from the BA, and the accompanying footfall, while POCL develop their long term vision - to be a provider of network banking services working as an agent to clearing banks as bank branch networks are shrunk;

- for BA it offers reductions in fraud (though much of this could be achieved through other means), but delays the move to ACT which will significantly reduce the administrative costs and risks involved in paying benefits.

14. Graham Corbett recognised this in his report, and the problems this caused to the incentives on the parties. He advised that, if Ministers proceed with the project, the contractual arrangements should be simplified leaving ICL with a direct relationship with POCL alone (and BA in turn contracting with POCL), once the automation platform has been rolled out.

15. The key issue now is whether Corbett's recommendations would still be enough, and whether we could in fact see the project through to successful roll out. Treasury officials do not believe they are. The project will not succeed against the background of dysfunctional relationships between the parties. Crucial to this we believe is the view of ICL, given that, under the terms of the PFI deal, ICL bear the risk if the project is not successfully delivered (i.e they receive no payment from BA and POCL until then). Initial indications are that Ministers would be hard pressed to persuade ICL to continue with the project

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under the current contractual relationships. To trigger payment, ICL have to satisfy both POCL and BA that the system is performing. Since December, there have been further disagreements. POCL had deferred the final run of testing by 2 months to allow ICL to fix the major problems. BA are not yet satisfied that all problems have yet been identified or resolved: the routine testing has thrown up a number of new faults in the system. ICL and POCL contest this view. ICL have indicated to us that they would now be reluctant to continue to invest in the Benefit Payment Card while the risk remains that POCL and particularly BA would not in the end accept it.

16. Treasury officials therefore believe there is a very strong risk that, even if Ministers decide in favour of Option A and can persuade BA to accept it, they will not be able to persuade ICL to continue with the project. In addition, Treasury officials judge that relationships within the project are now so dysfunctional that Ministers could take little comfort that Option A as currently configured would be delivered.

The alternative option

17. The objective of the discussions led by Steve Robson was to try to find a solution which removed the Benefit Payment Card from the project and moved directly to a system in which benefits were paid via ACT while seeking to maintain post office footfall revenue at a similar level to that achieved with the BPC, and which introduced more quickly a smartcard that could form the vehicle for Modern Government services. Of the options examined by the parties, the most promising method of achieving these objectives (known as Option B1) was as follows:

- the Benefit Payment Card is cancelled;

- POCL (or a specially-formed subsidiary) would provide simple "benefit accounts" into which benefits were paid via ACT and withdrawn in cash using a smartcard at post offices (if necessary POCL would seek authorisation under the Banking Act);

- these accounts would not offer other conventional account services (e.g. transfer of credit from another account, withdrawal at ATMs) and would appear to the benefit recipient very similar to the benefit payment card;

- BA would transfer benefits to POCL via the BACs system - in the same

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way as is currently done for benefit recipients who receive payment by ACT;

- POCL would contract with ICL (i) to deliver and operate the IT infrastructure required, and to manage the smartcards, using the existing Horizon infrastructure; and (ii) to administer the accounts;

- ICL would sub-contract with a bank (e.g. Girobank) the scope relating to administration of the accounts;

- POCL's aspirations to become an agent for the banks ("network banking") would be developed in parallel, as under option A.

Progress with Option B1

18. Good progress was made to work up Option B1. In a matter of weeks, this new concept was developed into a technical specification, and in turn translated into a fully worked up draft heads of agreement which is now close to being ready for signature - although there are a number of commercial and contractual issues to be resolved.

19. However, the major problem with Option B1 is the cost. Working on information provided by the parties, KPMG have modelled the NPVs of Option B1 to compare it with the Benefit Payment Card (Option A). The results reveal that Option B1 is estimated to be between £700m and £870m NPV lower than Option A (the higher figure reflects ICL and POCL's current "base" position - i.e. the assumption in their draft heads of agreement - that the new system could not be rolled out until July 2002). This is against an overall NPV of Option B1 of only £399m to £570m.

20. The main reasons for the differences in cost of option B1 relative to option A are as follows:

- by abandoning the benefit payment card we save around +£100m NPV (mainly reduced ICL costs);

- but this is more than offset by additional costs, which are (in NPVs):

    - foregone administrative savings to BA from abandoning the BPC and continuing with paper-based systems for longer: -£190m;

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- costs to BA brought forward from moving to ACT earlier than under the BPC: -£265m:

  - these reflect steady state costs of around £80m p.a. associated with ACT (largely driven by £50m p.a. cost of reviewing claimants to address entitlement fraud) which are not incurred under paper-based or BPC options; plus some upfront costs associated with moving to ACT as the primary means of payment which peak at around £35m;

  - from BA's perspective these additional costs are more than offset by the savings made from reduced payments to ICL of £372m NPV and reduced payments to POCL of £973m NPV;

  - but from the public sector's perspective, these savings are in large part a transfer payment since POCL and ICL have a large fixed cost base, and therefore must replace around 70% of their income in order to achieve an overall NPV equivalent to option A.

- providing a smartcard rather than a magnetic stripe card: -£70m;

- banking operation costs incurred by POCL and ICL of around -£240m (a large element of these costs will be subject to competitive tender - however Girobank (who may not be interested in the business) have provided an estimate which is higher than this).

21. In summary, the costs of option B1 are high because the public sector is effectively paying twice. It pays once to roll out the BPC system (albeit without the BPC), ensuring that POCL and ICL are able to achieve the same NPV as under option A. Given POCL and ICL have high fixed costs this involves replacing a large part of the revenue stream they would have received from BA. Secondly, the public sector must pay to establish and operate the new "POCL bank" system.

Possible revenue streams

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22. Against these costs there are additional benefits to the public sector which are harder to quantify, but nevertheless might still leave B1 offering value for money:

- Option B1 brings in a smartcard more quickly than Option A as currently configured; and

- B1 also introduces new contractual relationships which provide better incentives for the parties to act together, and which would simplify the decision-making process, thereby making the project more likely to be delivered successfully.

23. DTI and POCL have been considering possible revenue streams from pursuing this option which might offset the additional £700-£870m cost, although we haven't yet seen a paper summarising their views.

24. When considering the figures that emerge from DTI/POCL, the following should be noted:

- these revenues arise from (a) the automation of PO Counters and (b) the development of a smartcard. To that extent, they are available, although to different timescales, under *any* option that delivers these two elements - which in principle could be Option A or an alternative, non-ICL solution, if these options could be made to work;

- POCL themselves see this revenue stream as a future source of income to replace declining revenue streams from traditional sources . They do not have sufficient confidence in these revenue flows to fund the cost of rolling out the system - and are therefore not prepared to pay any of the costs of roll out - a position they have consistently held.

25. <u>The magnitude of the cost differential between Option B1 and the alternative options is great and considerable uncertainty surrounds the revenues (which in any event could be achieved under other options). POCL have said that they are unprepared to fund the additional cost. Imposing option B1 on POCL would be unsuccessful as POCL would have no ownership of the project. Treasury officials do not believe that, in the circumstances, it makes sense to proceed with option B1.</u>

<u>A non-ICL solution</u>

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26. Given the position on Option B1, and the doubts over whether Option A can actually be delivered, Treasury officials believe that termination of the contract with ICL to pursue an alternative strategy is the best way forward for the public-sector collectively. Obviously, this option is not one that any of the public-sector parties welcomes and indeed we have all expended substantial efforts to explore the alternative options presented here and others.

27. Under this option, the current Horizon contract would be abandoned. In order to retain footfall at post offices, BA would continue to pay beneficiaries with the paper-based methods until such time that POCL had the capability to offer customers an encashment service at post office counters. Once POCL has this capability in place, then BA would commence a process of migration of beneficiaries to ACT. As a separate and uncoupled effort, POCL would move-up on their longer-term vision to offer simple financial transactions at post office counters as an agent operating on behalf of banks and other financial intermediaries. POCL would undertake a fresh effort to procure an automation platform that could then be better tailored for the capabilities required to offer a valued service to prospective partner banks, which neither Option A nor Option B is optimised to do. DSS/BA would need a firm timetable for the migration of benefit payments to ACT, and a contract with POCL that appropriately incentivised POCL to meet this timetable.

28. On the face of our value-for-money analysis, this option looks to be of the order of £270 million lower (ie, worse) NPV than Option A, but better value for the public sector than Option B1. However, as already noted, these figures take no account of the delivery problem with Option A . The termination figures assume a settlement payment to ICL of £150m NPV. The NPV of this option is very sensitive to the timing of BA's move to payment by ACT, which results in foregone administrative and fraud savings of around £260m p.a. (although from POCL's point of view, this would give them more time to put in place their banking strategy and so would be less risky). The lower value relative to Option A could be eroded by the further delay in delivering the Project and, indeed as already noted, there is evidence to suggest that further delay and loss of value to the public sector is likely to occur (possibly of the order of up to a further £110m NPV for a six month delay).

29. The more time that elapses before the public sector exercises its right to terminate for ICL's breach the more likely it is that the public sector's case in litigation is weakened and therefore this option should not be deferred indefinitely.

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30. It may well prove possible to salvage the Horizon automation platform for POCL (without benefit payment capability) as part of the settlement negotiations with ICL stemming from termination of the contract. This could improve the NPV. Treasury officials believe that for the public sector to have any prospect of paying a fair and reasonable price for any such infrastructure, it would be necessary first to invoke the contractual right of the public sector to terminate for breach. In the absence of termination, an attempt to negotiate a procurement of those elements of the Horizon Project that are valuable to POCL will flounder due to ICL's expectations of being compensated for the total costs it has incurred to develop the infrastructure (of which a large part of the effort relates to benefit payments). And POCL have no real incentive to pursue an alternative approach making use of the Horizon infrastructure (whether some form of option B1 or an alternative) until option A is firmly off the table.

31. Treasury officials recommend that the best way forward would be to make a clean break and allow the contracts with ICL to be terminated, in order to pursue a strategy that better met the needs of the public sector at a reasonable cost.

DTI and Post Office views

32. DTI officials and the Post Office do not agree that termination is the best way forward, as set out below.

33. Termination of the project would undoubtedly be a major blow to ICL. Just how great would depend primarily on the stance taken by Fujitsu who have claimed that it could lead to the collapse of ICL. At the very least it would seriously jeopardise Fujitsu's plans for ICL's floatation next year, and could lead Fujitsu to decide to divest itself of the company. Even on a "least bad" scenario of an agreed termination, the failure of the project would badly damage ICL's reputation both here and in export markets and its future prospects. DTI officials are also concerned about the effect that termination could have on our relations with Fujitsu. Fujitsu have been a major inward investor in the UK, with well over £700m invested in the last decade and the creation of around 20,000 jobs. Whatever the justification from a UK standpoint, termination would be seen in Tokyo as a major breach of faith by the UK Government - a withdrawal from the project because we had changed our minds on the policy but had sought to put the blame on ICL. It also risks being seen in some quarters as a vindictive retaliation by the UK Government

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against Fujitsu for the latter's closure of the Newton Aycliffe plant in the Prime Minister's constituency.

34. From a Post Office viewpoint termination now would delay by at least two or three years the availability of the modern, on-line automated platform which POCL desperately need if it is to retain existing clients and to win new business. Loss of the benefit payment card and the Horizon platform would be seen by the 18,000 sub postmasters as a devastating blow to their commercial prospects, and no matter now carefully managed the announcement, many would simply give up. The value of post office franchises would plummet, and replacement franchisees would simply not be available. The effects of these unplanned closures on the integrity of the network as a whole can only be guessed at this stage, but could be serious.

35. They could well be sufficient to cause existing and prospective clients to re-evaluate the value of the network as a delivery mechanism. Under any such scenario, the true costs of termination would rapidly escalate to a point at which they significantly exceeded the cost of proceeding with either Option A or B.

36. The Post Office remain firmly of the view that despite the difficulties referred to earlier in this report, Option A remains their preferred way forward. The assured revenue stream for a further period of years, the highest retention of footfall, and a smooth and controlled migration at ACT and network banking mean that this option offers POCL the best prospect of transition to a viable commercial future, free from the need for Government subsidy, and with the delivery of a unique interface and channel of communication between Government and the citizen.

37. DTI officials also believe that the present unattractive profile of Option B1 may be significantly softened once an assessment of the revenue stream which POCL could expect from the commercial exploitation of the Horizon platform.

38. Finally, the delay which termination will cause to the availability of a modern online automated platform capable of delivering front end banking facilities on behalf of the commercial banks will, if serious damage to the Post Office Counters Network is to be avoided, delay the move from present paper based methods of paying benefits by at least two or three years.

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Reform of POCL

39. Treasury officials believe strongly that we should place little confidence in the existing management of POCL to successfully achieve any of the options outlined above, including the adoption of an effective strategy and new IT project following termination. All would require radical reform to the management of POCL. What we would have in mind would involve:

- bringing in new management from outside of the Post Office. They would be paid according to their success in growing the POCL business. We would need to look at the scope for strengthening POCL as a separate entity, with autonomy from the Post Office board;

- creating strong incentives for change within POCL in order to protect the taxpayer - through restructuring of the funding of POCL to provide incentives to deliver network banking and electronic government services successfully.

This would represent radical reform. But we judge that this is the only way that any way forward could be made to work.

The Way Forward - termination of ICL contract and pursuing an alternative solution

40. If you decide to pursue a non-ICL solution then the next steps are:

- for Steve Robson to meet the Chairman of ICL to thank them for their efforts to find an alternative way forward, but to break the news that neither ICL's December offer on continuation, nor the alternative option are acceptable. They will probably not be surprised;

- to seek to reach a negotiated settlement with ICL, possibly involving salvaging some elements of the project (but this would be for POCL to negotiate with ICL);

- to set in train the necessary legal process to move towards termination of the existing contracts either (preferably) by negotiating an agreed termination or by serving notice of termination if ICL is not willing to negotiate;

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- for the Prime Minister to speak to the Chairman of Fujitsu to express his regret but provide as much comfort as possible in the circumstances that the Government remains fully committed to Japanese inward investment;

- to prepare to make a public statement on the future of the project to provide reassurance to benefit customers and subpostmasters in the event that the story breaks.

41. On a slightly longer timescale, we suggest that:

- restructuring of the management of POCL is taken forward;

- POCL are given a clear and urgent timescale to work up their network banking and citizen smartcard strategy and to decide what infrastructure is necessary to deliver this - drawing on advice from the retailing and banking industry;

- DTI with HMT consider how POCL can best be incentivised to deliver their worked-up strategy successfully and as quickly as possible (given that the later BA move to ACT, the greater the foregone savings to the public sector);

- linked to this timescale, we provide BA with a firm end-date by which time they will be allowed to move to ACT directly into bank accounts as the primary means of payment of benefit (which would at the limit be no later than currently envisaged under option A - ie 2005).

A "three-pronged approach" setting out possible objectives for a negotiated settlement is suggested at Annex B.

<u>Legal process</u>

42. Lawyers acting for DSS and POCL could not agree on the best way to achieve termination. The two options suggested were:

- to serve a 3 month notice terminating the contract;

- to serve notice making time of the essence - which would have to be a reasonable period, and could be up to 9 months.

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43. Ministers therefore agreed that the Treasury Solicitor should seek the advice of the Law Officers last December. His advice was that if Ministers unequivocal wish was to terminate (i.e. to offer ICL no prospect of delivering the existing contract) then they should serve a 3 month notice terminating the contracts. This route is the quickest route to termination (although it involves additional legal hurdles and carries a greater risk that the public sector parties would be held in breach of contract and thus liable for damages). There is some advantage in the light of recent developments in not serving notice immediately to allow time for a negotiated termination. If this approach is adopted, it would be important not to say publicly that the public sector parties have terminated the contracts, as the form of public statement to be made about the reasons for cancellation of the project will be a valuable bargaining chip in settlement negotiations with ICL.

<u>Presentational Strategy</u>

44. The handling of an announcement will in part depend on the reaction of ICL and Fujitsu to the news that continuation options are unacceptable. If ICL are prepared to seek a negotiated settlement then part of our negotiating leverage will be how termination is presented publicly. If, however, they intend to litigate, then the Government will have no alternative but to make it clear that termination was due to failures on the part of ICL to deliver to time or budget- despite the best endeavours of the public sector to find a way forward.

45. A key concern in any event will be to reassure subpostmasters about the future of their businesses. The Horizon project has, in the past, been portrayed - by the Post Office, by Ministers and by the National Federation of Subpostmasters - as the vital element to secure the commercial future of the counters business. News that the project is to be scrapped will be a severe blow to subpostmasters' confidence, unless an alternative approach is outlined at the same time. Ministers will therefore need to stress:

- the Government remains fully committed to a nationwide network of post offices - and fully recognises the importance of post offices to the communities they serve;

- the Government is equally committed to the automation of post office counters, and the Post Office has already begun work to secure a replacement, which will give it the potential to seize new opportunities -

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for example the provision of network banking services and electronic government services;

- there will be no change to the existing arrangements for the collection of benefits in cash at post offices.

46. The Government will also want to reassure benefit recipients that they will continue to be able to collect their benefits at post offices; and to explain arrangements for withdrawing the BPC from the early customers using it. In addition it will be important to convey the message to the IT industry and Japanese inward investors that the Government has acted in good faith.

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ANNEX A: IMPACT ON THE PUBLIC SECTOR

£m NPV	option A	option A (6 month delay)	option B1 - ACT from Sept 2001	option B1- ACT from July 2002	Term'n of ICL contract (ACT in 2001/02)	Term'n of ICL contract (ACT in 2003/04)
BA	1,123	1,005	2,108	1,805	2,087	1,237
payment to ICL[1]	(36)	(59)	(395)	(439)	(150)	(150)
POCL	179	212	(1,143)	(966)	(943)	(619)
total NPV to public sector	**1,266**	**1,158**	**570**	**399**	**994**	**468**

[1] For option A and B1 this assumes that ICL are compensated to ensure they achieve -£126m NPV overall (offer of December 9/18). For Termination, the modelling assumes a settlement to ICL of £150m NPV.

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ANNEX B: Possible Elements of Termination and Settlement Strategy

1 **ICL Settlement**

Public-sector parties pursue a settlement with ICL involving:

A Procure the components of the Horizon that are valued by POCL as an automation platform for their core products (excluding payment of benefits);

B Procure the OBCS elements of Horizon but exclude other elements relating to the Benefit Payment Card;

C The procurement for the above from ICL would not be on the basis of ICL taking transaction volume risk but instead on a fixed/variable fee with performance incentives and penalties;

2 **POCL Restructuring**

POCL immediately commences a restructuring of its business:

A Management of POCL is strengthened and an incentive compensation structure introduced to attract and retain a commercially-oriented talent base;

B As a high-priority precursor to enable BA's migration to ACT, POCL obtains the capability to offer a simple cash-back service to customers through an existing commercially available system (such as Link or Switch);

C Develops plans to rationalize the post office network with a view to obtaining substantial reductions in running cost commencing in 01/02;

D Develops a detailed plan (including schedule) to market its counter services to prospective partner banks;

E Develops a plan to aggressively exploit the opportunities presented by Modernising Government through a Post Office branded smart-card and a national network of automated Post Offices.

3 **Benefits Agency Payments**

A BA continues with orderbooks and the related payments to POCL until POCL has achieved national roll-out of its basic automation infrastructure and implemented the commercial arrangements necessary to offer customers cash from a bank debit card;

B BA develops a detailed plan for migrating beneficiaries over to ACT at retail banks (including addressing the plan for dealing with those rejected as unbankable, or incapacitated or otherwise unsuited for ACT) -- migration to be launched when the POCL infrastructure to provide cash from bank debit cards is in place;

C BA will actively advise and reassure beneficiaries that they will be able to obtain cash using their bank debit card at POCL and that there will be no customer charge for obtaining cash in this way — transaction charges incurred by POCL to the third-party clearing system will be reimbursed by BA (ie, POCL incurs charge, not the customer, and BA reimburses POCL).