

PO BOARD MEETING 19/20 JULY 1999BA CONTRACT NEGOTIATIONS-BACKGROUND BRIEFING**1. Contract Terms and Conditions****1.1 BA Position:**

BA claim to have a negotiating remit from their Minister that is based on the assumptions in the KPMG modelling exercise which was used to inform Ministers on the value for money of the various options being considered around the future of the programme. Principally these are:

- a price for the Order Book Control Service based on the previous contract with ICL. This was a marginal price that resulted in income to POCL of c £103m over the life of the contract. The charging arrangements from which that price was derived do not exist anymore.
- loss of the minimum guaranteed payment mechanism in the current contract between POCL and BA (KPMG assumed this disappeared from 2003/4 when compulsory ACT came in. However BA maintain this was meant to be with immediate effect). This would reduce POCL's income over the life of the contract by at least £200m. There is also a risk that with the removal of the minimum guarantee payment immediately, BA would actively and possibly covertly seek to transfer payments to ACT and reduce volume through POCL - this despite Ministerial assurances to the contrary.
- It is worth noting BA's position, that their Minister does not want to be responsible for the funding of the Post Office/Network.
- BA also maintain that their Minister was asked to state what level of payment he could support, by Treasury Ministers, at the time that the decision was made about the future funding of the programme and he used the KPMG numbers. (It is quite clear from the notes in the KPMG report, that BA provided the assumptions that were used in the modelling of the option we are going forward on - in isolation from either POCL or ICL. Furthermore it is also clear that KPMG tempered some of those assumptions i.e BA wanted to reduce POCL's fixed price when the move to ACT started) BA therefore say they do not have the funds to pay any increased charges.

1.2 POCL position:

- POCL claim that as a result of the revision in contracts - arising out of the termination of the Payment Card - the cost of providing automated services has increased. It is looking to BA to pick up its fair share of

costs for the OBCS services which use up a very significant share of system capacity etc. POCL is seeking c £300m for this service over the life of the contract. (The difference between our positions on price is £200m) If BA do not pick up a fair share of the costs then in effect they are being subsidised by the Post Office!

- On the issue of the minimum guaranteed payment disappearing with immediate effect, POCL have pointed out the inconsistency in BA's arguments that this was a KPMG modelling assumption.
- POCL's position is that BA should honour it's current contract which includes the floor till 2005. Furthermore the floor was part of a pricing package (ie generous RPI-x) over the life of the contract and if BA wish to re-open this element of the contract then the whole package needs to be reviewed. Without a clear understanding of BA's ACT plans it is not possible to understand what the implications are for POCL in terms of infrastructure costs. The floor provides some stability.

2 Acceptance

2.1 BA Position:

- BA want to mirror POCL's contractual position with ICL on Acceptance/roll-out (and service provision) in their own contract with POCL.

2.2 POCL's Position

- POCL accepts entirely that BA, as a customer for OBCS, must be able to satisfy itself that the service meets its requirements and is fit for purpose. However the model it would prefer to use is one which it has already adopted successfully with BA in the past for the ALPS/ESNS service as well as its other Bill Payment clients i.e client requirements are specified and POCL provides evidence and assurance that those requirements are met involving the client where necessary. The contract is managed through Service Level Agreements and there are penalties within that for failure to perform.

POCL feel that in seeking to replicate the Acceptance arrangements that were previously in the ICL contract (some of which have changed since codification) and asking for the same level of protection that POCL has from ICL in terms of remedies, liquidated damages etc, BA is wanting to retain the privileges of being a Contracting Authority without any of the costs and risks. Furthermore OBCS is far less mission critical than the Benefit Payment Card. However BA may try to talk it up, OBCS is an electronic stop notice facility. They should not therefore have the right to demand assurances about all aspects of the

ICL system and its operation on the basis of their paying POCL for this service.

- There is also some evidence from the demands we have had from BA - in terms of Acceptance - that they are attempting to increase their requirements so as to make the service replicate some of the benefits of the Payment Card. POCL has made it clear that any change in requirements needs to be dealt with under change control procedures.
- The obligations that BA's approach on Acceptance would place on POCL could result in increased costs and liabilities and also allow BA the opportunity to interfere in the acceptance process where all the risks of increased costs and delay to Programme time-scales are borne by POCL. As an illustration were to accept BA's proposals, a worse case scenario might be one where POCL accepts the whole service from ICL, but in its mirror acceptance process with POCL, BA refuse to accept the OBCS service thus placing POCL in an invidious position on a decision to roll-out. If POCL did so at its own risk, BA could refuse to pay for the service and claim damages from POCL for failure to complete the operational trial successfully.

3. Current Position

The impasse on the negotiations in terms of the price for OBCS and removal of the floor has been drawn to the attention of Ian McCartney through the Committee he chairs and at his request we have written to him to brief him on the position and seek his assistance. He has written to Alistair Darling who has agreed to a meeting.

We have not asked the Minister to negotiate a deal- simply to ask Alistair Darling to remove the self imposed financial constraints on his team so that a proper commercial negotiation can be conducted between BA and ourselves. However there is always the risk that he will attempt to a deal and therefore careful briefing will be provided. In the meanwhile, the Board should be made aware of the above and hopefully they will support our stance that:

- (i) BA should not be granted contractual status on Acceptance that exactly replicates that between POCL and ICL and;
- (ii) If necessary and Ministers are unable/unwilling to help and BA hold out on paying a fair price for OBCS, POCL can refuse to provide the service when it rolls out. It will be important to be able to demonstrate that POCL is serious on this point if we are to get any movement.