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SLAUGHTER AND MAY

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Horizon

I have had a look at Sarah Graham's draft reply to Fujitsu on behalf of the British Ambassador in Tokyo.

First, I agree that a reply should be sent refuting the various claims made. However, I feel that the draft reply goes into too much detail and, more importantly, allows the reader to infer various admissions of liability, for example:

- (a) "the public sector is in no material respect responsible" equals "the public sector is responsible to some extent";
- (b) "the assertion is unsupported" equals "the assertion could well be right but ICL has not proven it yet";
- (c) "there is no documentary evidence" equals "it may be true, and there may be evidence that it is true, but we have not seen it in writing yet";
- (d) "Since that time, the BA has met all of its obligations" equals "before that time, BA was at fault."

I am not suggesting that these conclusions would all necessarily be drawn from the words and would not be capable of being rebutted. However, it seems unnecessary to be less than forthright in our denials. We should also resist going into too much detail.

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Against this background I attach a proposed mark up of the letter.

Regards,

GRO

Jeff Triggs

cc. Nick Gray, Slaughter and May

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RESTRICTED - COMMERCIAL & POLICY

draft 9/12/98

**LETTER FROM CST IN RESPONSE TO NARUTO'S LETTER OF 4 DECEMBER TO
SIR DAVID WRIGHT****BA/POCL AUTOMATION PROJECT**

✍ Thank you for your letter of 4 December to Sir David Wright about the PFI project to automate benefit payments and Post Offices. Sir David has passed your letter to me, as the Minister responsible for co ordinating the cross-Government review of the project.

~~2. First, I was struck that there seemed to be a number of areas where there are mis-~~
understandings about the facts and events which have led to the HM Government's current discussions with ICL and ICL Pathway about the future of the project. For clarity, I have set out HM Government's view of the points raised in your letter in the attached note. I hope ~~you find this helpful.~~

✍ ~~More generally,~~ I can only emphasise HM Government's clear view that ICL Pathway ¹⁵ ~~are~~ in default for failure to deliver a key operational milestone for which they were placed ^{it was} formally in breach in November 1997; that the public sector ~~is in no material respect~~ ^{is not} responsible for the delays; that, given the importance of this project to Government, to ICL and yourselves, and not least to the British people who are the ultimate customers for it, we have been making every effort to find an acceptable way forward: but that so far, ICL ~~have~~ ^{has} made that difficult for us. HM Government cannot justify using taxpayers' money to meet the costs of ICL's failure to deliver; nor would it be fair to do so, given the nature of the competitive tender on which the contracts were first let. ~~Finally, I should point out that the public sector have made all the significant financial moves so far in our attempts to find a way forward, and it is against this background, that I and my colleagues are now looking for a significant move on the part of ICL.~~

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~~4. It is in this context that we will be viewing the proposals which we have just received from ICL, and we will be expecting to let them have our decision very shortly.~~

~~5. I hope this letter helps to clarify the position.~~

STEPHEN BYERS

I am delighted that Fujitsu is taking an interest in this contract but I wholeheartedly reject, on behalf of both public sector parties, the allegations and criticisms made in your letter.

We do very much hope that this matter can be resolved amicably and to the satisfaction of all concerned.

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RESTRICTED - COMMERCIAL & POLICY**Restricted - Policy and Commercial****DRAFT**

[Annex to letter from Chief Secretary in response to Naruto's letter of 4 December to Sir David Wright.]

Changes in specifications

The assertion that the sponsors instigated many changes to the technical specification, thereby causing the delays which have beset the project, is unsupported. There have been no significant changes in the sponsors' requirements and the volume of changes to technical specifications sought by ICL Pathway and the sponsors is no more than would be expected of project of this size and complexity. The decision to award the contracts to ICL Pathway was based on the solution tendered by ICL Pathway in response to the sponsors' requirements. ICL Pathway's solution continues to be the sponsors' preferred solution. The sponsors are, however, concerned to ensure compliance with the contracted solution, subject to any changes agreed by all the parties.

Role of the Project Delivery Authority (PDA)

The suggestion that the PDA - established to manage the relationship between ICL Pathway and the sponsors - was unnecessarily bureaucratic, added to the delays and was subsequently abandoned following complaints by ICL Pathway, is unsupported. The PDA played an invaluable role in the management of the project and provided an essential single point of contact between ICL Pathway and the two sponsor organisations. It was, however, inevitable that the organisation would evolve as the project moved from the procurement phase to implementation. This resulted in the sponsors' proposal that the PDA should be reformed as the Horizon project. Indeed, there is no documentary evidence of ICL Pathway complaining to the sponsors about the role of the PDA. ICL Pathway, by contrast, found it necessary to bolster its own organisation, particularly in management, planning and testing areas, in recognition of its serious underestimation of the task to which it was committed.

Alleged failures of the Benefits Agency

The suggestion that the BA failed to meet its obligations under the contracts in the supply of data to ICL Pathway and that this has added to ICL Pathway's delays and costs is unsupported. In February 1997 all parties, including ICL Pathway, entered into negotiations to revise the project plans in recognition that all of the parties, including ICL Pathway, would have difficulty in meeting their obligations under the terms of the original contracts. The resulting plan was agreed on a no-fault basis. Since that time, the BA has met all of its obligations under the terms of the revised contracts to time except where there were dependencies on ICL Pathway and ICL Pathway was unable to meet its own commitments.

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Treasury Review

ICL refers to the review panel established in February 1998 under the auspices of my officials here at the Treasury, to provide an independent assessment of the project and to provide an added impetus to finding an acceptable way forward. We were very pleased that after some discussion ICL felt able to contribute, along with the 2 public sector parties, to that review, which formed a significant basis for the very careful consideration Ministers have been giving to the future of the project.

Benefits Agency's commitment to the project

ICL has suggested that the BA is a reluctant partner in this project and that this must cast doubt on the willingness of the sponsors to negotiate in good faith. We dispute this. Whilst the BA sees clear advantages in paying benefits via automated credit transfers into bank accounts, it also recognises that very many of its customers wish to go on collecting their money in cash at the post office. That is why the BA has fully supported this project by meeting all of its contractual obligations and by giving the project the very highest priority within its own work programme. We would also add that the sponsors have every interest in seeing the objectives of the project secured, not least to avoid adding to the costs which have already been incurred as a result of ICL Pathway's delays.

Increased costs to ICL Pathway

ICL has referred to its escalating costs and the difficulties it faces in financing completion of the project. ICL also suggests that it will need to secure commercial terms which will enable it to recoup its investment. But, as you recognise, this is a PFI contract under which the service provider agrees to bear substantial risks associated with design, development and implementation. The sponsors are firmly of the view that ICL Pathway has been in breach of contract since November 1997 for failing to complete an operational trial required under the terms of the contracts. As a consequence of this and other delays caused by ICL Pathway, both sponsors have incurred very significant additional costs. Any proposal which envisaged a transfer of risk back to the public sector would therefore be unacceptable in view of ICL Pathway's responsibility for the delays.