Report by the
Comptroller and Auditor General

Department of Social Security

The Cancellation of the Benefits Payment Card project

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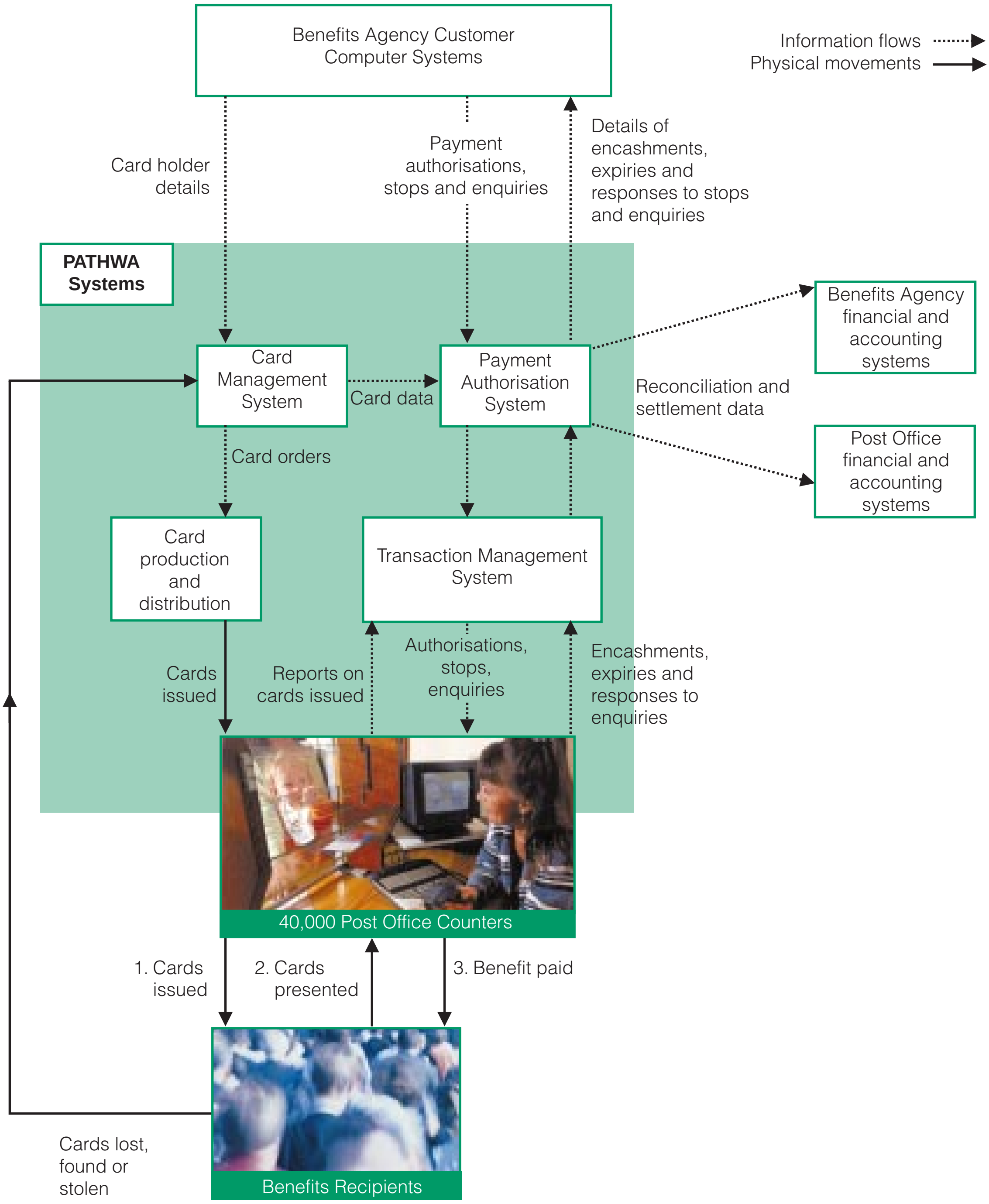
The Benefits Payment Card System - An overview

The Benefits Payment Card system was a large, complex system, linking transactions at Post Offices with the systems of the Benefits Agency and Post Office Counters Limited. The supplier, Pathway, was responsible for the issue and distribution of payment cards and the processing of transactions and enquiries.



Note: To ensure clarity, other functions particular to Post Office Counters Limited are not shown.

Source: National Audit Office

Executive summary

The Benefits Payment Card project was started in May 1996 and cancelled in May 1999 after continual slippage

1 In May 1996 the Benefits Agency of the Department of Social Security and Post Office Counters Ltd (the purchasers), jointly awarded a contract to Pathway, a subsidiary of the ICL computer services group. The Benefits Payment Card project was intended to replace by 1999 the existing paper-based methods of paying social security benefits with a magnetic stripe payment card, and to automate the national network of post offices through which most benefits are paid across Great Britain and Northern Ireland.

2 The project was vast in its scale and complexity, and estimated to cost some £1 billion in payments to Pathway. It was also one of the first Information Technology contracts awarded under the Private Finance Initiative. Under such deals the supplier receives a contract to design, build, finance and operate an asset, and is paid for the provision of the service only as it is successfully delivered. The purchasers, (the Benefits Agency and Post Office Counters Ltd), used the Private Finance procurement method because they did not expect to have the capital resources to develop the Benefits Payment Card themselves, and wished to transfer to the private sector risks of developing and delivering a working system and preventing fraud. The Department's business case for the project was based on achieving the potential fraud savings from introducing the new system. This meant that any significant delay in delivery would begin to erode the business case.

3 The overall objectives of the project were to:

- provide a virtually fraud-free method of paying benefits at post offices that was automated, had lower end-to-end costs than the current paper-based process, with continuously reducing overall administration costs year on year;
- extend automation to Post Office Counters Ltd's transactions for other customers, its products and its support processes to improve competitiveness, increase efficiency, and to enable greater commercial opportunities;

- enable full and speedy reconciliation of benefits payments, with accounting arrangements consistent with recognised accountancy practices; and

- provide an improved service to both purchasers' customers.

4 By October 1996 the contracting parties had successfully implemented a limited version of the system, which paid child benefit in ten post offices in Gloucestershire. Development work continued and further functionality was added through successive software releases which were used in 205 post offices. But designing and developing a fully functional system proved much more complex and took much longer than had been expected. The programme at the time the contract was signed assumed that it would take ten months to start a live trial of the full system intended to cover 24 different benefits and all of the 19,000 post offices then in the network. In fact, this stage had not been reached at the time the contract was terminated nearly three years later.

5 During the second half of 1996 the two purchasers and Pathway became increasingly aware of the difficulty they faced in developing the full payment card system. Discussions were opened that led in February 1997 to a "no-fault" replan of the project. Under this plan, all parties agreed to defer the final delivery dates by three months and to bear their own costs in doing so. Subsequently the Department introduced new customer accounting and payment systems covering four benefits and holding records of 16 million customers, releasing the software in time to link with equivalent phased releases of Pathway's new Card Payment systems.

6 Despite the replan, the project continued to make slow progress, for reasons explained in paragraphs 14 to 24 of this summary and in Part 3 of this report. Though Pathway delivered intermediate releases of software, by 21st November 1997 they had not completed, as required by the replan, a live trial to demonstrate satisfactory, sustained operation of child benefit payments and a range of Post Office functions in 300 post offices. The purchasers served on Pathway a formal notice of breach of contract, which Pathway denied and did not accept liability for, counter-asserting breach of obligations by the purchasers. In December 1997 Pathway wrote to the Benefits Agency suggesting that if the project were to continue they would either have to increase their prices by 30 per cent or extend the contract by five years and raise prices by five per cent.

7 The Department were not in a position to take unilateral action, but recognising the continuing difficulties, sought interdepartmental discussions involving primarily HM Treasury, the Department of Trade and Industry and the Prime Minister's office to reach a wider cross-government solution. Post Office Counters Ltd and Pathway were also involved. In July 1998, an independent panel of experts concluded that the project could deliver the functions required, but was unlikely to operate nation-wide much before the end of 2001, three years later than originally planned. They stressed that successful delivery would require renewed commitment from the parties and was not without risk. The cost of continuing was uncertain.

8 Discussions between government and ICL in late 1998 failed to close the gap between both sides' proposals for continuing the full project. From January 1999 discussions turned instead to the terms on which the automation of post offices could proceed without inclusion of the Benefits Payment Card.

9 In May 1999 the government decided that removing the payment card from the project offered better value for money than complete cancellation, would better protect the early automation of the Post Office, and was preferable to continuation. They devised a new strategy with the following key features:

- the Benefits Payment Card element of the project would be dropped, simplifying and assuring post office automation;
- automation of the Post Office would proceed, for completion by 2001;
- benefits payments would be made by automated transfers to claimants' bank accounts; starting in 2003 and completing by 2005. Until 2003 existing arrangements would continue;
- people who wished to continue to collect their cash at post offices would continue to be able to do so. The Post Office would introduce suitable banking technology and commercial arrangements with banks to allow this to happen; and
- for the relatively few people for whom a bank account may remain an unsuitable option, special arrangements would be made.

10 In June 2000 the Secretary of State for Trade and Industry announced a package of measures designed to modernise the Post Office network by;

- ensuring that benefits and pensions can still be paid in full, in cash at the local post office;
- setting up a special fund to improve local offices in deprived urban areas;
- providing help for those on low incomes;
- providing people with new opportunities to use the internet;
- encouraging post offices to act as Government one-stop shops;
- maintaining the rural network by placing a formal requirement on the Post Office to prevent any avoidable closures of rural post offices; and
- supporting the development of the proposed "Universal Bank", giving banking facilities for up to 3-5 million extra people, and allowing customers, including pensioners, to get cash out of the post office and set up direct debit arrangements.

11 The delays to the Card project and its subsequent cancellation affect benefit claimants, the Department of Social Security, the Post Office and ICL. These consequences are described in Part 1 of this report.

Scope of our examination

12 We have examined the conduct of this project to identify:

- the reasons why the Payment Card project failed to meet its objectives; and
- whether there are useful lessons that should be learned for other projects; particularly in terms of the approach taken towards the management of risk.

13 The project was a tripartite venture, requiring all three parties involved to meet their contracted obligations for the project to be successful. This report, however, focuses on the role of the Department of Social Security in the project. The Treasury and the Department of Trade and Industry, which sponsors the Post Office in central government, were also actively involved in reviewing the project and in the decision to cancel the Benefits Payment Card, taking account of the wider interests across government. The Comptroller and Auditor General has no statutory rights of audit access to Post Office Counters Ltd, but in the interests of completeness and balance the report refers to the objectives and involvement of Post Office Counters Ltd in the Payments Card project and the consequences for them of its cancellation. The Comptroller and Auditor General had certain rights of access to records held by Pathway for the purpose of examining the value for money with which the Department of Social Security used its resources, and Pathway co-operated with us in our examination. Our approach towards the examination is described in Appendix 1.

The project was high risk. It was feasible, but probably not fully deliverable within the very tight timetable originally specified

14 The project was an ambitious one, and with hindsight, probably not fully deliverable within the very tight timetable originally specified. It had special features that added to its risks; notably its status as a pioneering Private Finance Project, the need to join up the systems of two purchasers with differing business objectives, and the need for the development and testing of more new software than was originally envisaged.

Key Statistics of the Project

Estimated contract value, (Payments by Department and Post Office):	£1 billion, net present value over 7 years
Number of post offices to be equipped:	Up to 20,000, with 40,000 counter points in Great Britain and Northern Ireland
Number of post office staff to be trained in use of the system:	67,000 staff, serving 28 million customers per week
Number of social security benefit recipients to be issued with Payment Cards:	17 million, claiming some 24 different benefits
Number and value of benefit transactions:	In 1999/2000 some 760 million payments worth £56 billion were made through post offices

The project was procured through an innovative method

15 As a ground-breaking Private Finance project in the Information Technology sector, there was little by way of precedent to inform it. There was limited experience at the time as to the appetite and ability of the purchasers or potential suppliers to accept important risks, such as the liability for failing to prevent fraud. There was also a perception that because responsibility for delivery could be transferred to suppliers, purchasers should be less concerned with validating the supplier's internal arrangements and had less "need to know" the detail of the supplier's solution.

The Department and Post Office Counters Ltd had different objectives for the project. These were not incompatible but they led to tensions which required a genuine partnership between the two purchasers to resolve.

16 The objectives of the Department of Social Security and Post Office Counters Ltd in undertaking the project were different, reflecting their different business drivers. They rightly agreed a memorandum of understanding between themselves before signing the contract with Pathway, which addressed their commercial relationship. But this did not prevent later disputes on matters of detail. For example, arrangements that the Department wanted to ensure security for payments to people temporarily collecting benefits on behalf of claimants proved difficult to balance against Post Office Counters Ltd's commercial interests in maximising the flow of customers through its outlets.

17 We found significant evidence that the Department had shown commitment to the success of the project. In 1997/98 they employed up to 1100 staff plus consultants in designing and implementing their CAPS computer systems that were to link to the Payment Card. They also agreed to the system being installed in 205 offices without the full range of contracted security features. In late 1997, when the project was clearly in deep trouble, they sensibly began contingency planning for a possible implementation of payment by bank transfers, in case the Benefits Payment Card project should fail. Pathway told us that they felt that the Department's commitment had reduced from around this time, in their view because the project no longer had such strong champions within the Department as before. Argument over difficult issues, mainly to do with how best to ensure the security of the system, tended to raise doubts among the participants as to their partners' commitment to timely delivery of the project. Similarly, because Post Office Counters Ltd had a lower financial incentive than did the Department to achieve a quick changeover from order books to the Benefits

Payment Card, the Department at times questioned their partner's motivation. Post Office Counters Ltd insist that they too had a strong interest in playing their full part in delivering the entire project to time. In our view, such doubts about partners' commitment inhibited a genuinely open and participative approach to tackling the severe problems of the project.

The Department's initial business case did not adequately assess the risk and costs of serious slippage

18 The Department's business case for the project was based on achieving the potential fraud savings from introducing the new system. This meant that any significant delay in delivery would begin to erode the business case. The misuse of order books and girocheques was at the start of the project estimated to cost the taxpayer over £150 million in fraud each year, though from 1996 a system of electronic stop notices implemented in the London area started to reduce this. Payment fraud losses are now estimated at some £100 million. We found that the Department's business case for the project included limited analysis to ensure that it would remain robust in the event of significant slippage. The Department accepted that slippage presented a risk to their business case, but were confident that a large proportion had been transferred to Pathway, who were to be paid only when the service was up and running. Sensitivity testing was done routinely after signature of the contract to assess the impact of revised dates.

The purchasers, the Department of Social Security and Post Office Counters Ltd, established arrangements to manage the risks of the project, though with only limited success

The purchasers identified most of the risks of the project, but were less successful in assessing their probability and impact

19 The purchasers' joint procurement team made strenuous efforts to identify the risks of the project. In March 1995 they compiled a register comprising 224 risks, including virtually all those that could have been foreseen and those that eventually impeded the delivery of the project. However, this register did not include assessments of each risk's probability and impact, nor did it allocate risks to "owners" for management, or propose options to manage the risks. We found no evidence that this formal register was subsequently further developed and actively used in the project, though some of the risks it contained were identified again in subsequent registers later in the project.

20 We found that the purchasers' process for selecting a supplier was diligent. Considerable resources, effort and care went into the evaluation of bidders' proposals, and we found no indication of any impropriety. In mid-1995 the procurement team produced separate risk registers for each of the three shortlisted bidders based on their detailed technical proposals, demonstrations of capability and subsequent negotiations. This approach was fundamentally sound. But though risks were assessed for impact and probability of occurrence, there were significant risks in Pathway's proposals that the procurement team's register did not address. These included risks to delivery from very ambitious proposed timescales for system development and testing, to meet exacting deadlines for implementing the Payment Card, and a lack of information on the resources that Pathway would apply.

When the contract was signed key parts of the detailed specification had not been finalised

21 All high level specifications were agreed ahead of the issue of the Invitation to Tender. However, a decision not to complete the documentation of both purchasers' detailed requirements before contractor selection and contract award was a major contributor to the later problems of the project. The decision was agreed by the joint project board and by the shortlisted bidders, and recognised Ministers' legitimate interest in proceeding with implementation of their policy for the payment of benefits.

22 When the contract was signed much of the detail of how the development and operation of the Card was to be provided had not been agreed between the purchasers and Pathway. From the records it seems that there were some 289 agreements to agree the detail of the service contained in it, of which 38 remained to be agreed by Pathway with the Department of Social Security, 124 with Post Office Counters Ltd, and 127 with both clients jointly. Some of these matters were relatively minor, such as the design of the logos to appear on the card, whereas others, examples of which are shown in Appendix 2, were more significant. Pathway told us they had expected them to be cleared within three months and that when this did not happen they obtained a contract amendment exonerating them from liability for any delays that were a direct consequence of failures to agree. The number of outstanding agreements to agree reduced greatly during the implementation phase. But vital issues, such as the precise nature and specification of the system's security procedures and reports, particularly how these would adapt to changes in patterns of fraud, remained unresolved when the Card project was cancelled three years later. The Department agreed to Pathway's

request to defer full implementation of these security procedures, providing they were fully in place before rolling out the system for higher risk benefits than Child Benefit, such as Income Support.

More rigorous demonstrations by bidders might have better highlighted the risks to deliverability and the extent to which new software had to be developed.

23 One reason why risks to delivery were not properly assessed was the limited scope of the demonstrations mounted by the shortlisted suppliers to show the viability of their proposed solutions. In the case of Pathway this was a demonstrator system based on one already operating in the Republic of Ireland but meeting a requirement much simpler than the Benefits Payment Card. The other two bidders constructed mock-ups of new systems. Though the purchasers had at one point considered a fully-fledged pilot stage, this was not done for reasons of cost and time. There are limits to how much further work bidders will do in such circumstances without funding from the purchaser.

24 This project initially proceeded on the basis of proposals from bidders that it would involve mainly the integration of existing software packages. In the event, the greater than expected complexity of the service requirement obliged Pathway to develop much more new software than they had planned. The Department's view is that Pathway knew what was required but had intended to fit the requirement to match a system they had already implemented in Eire. The extent of new software development had major implications for the degree of difficulty of the project, since this is a high-risk activity with high failure rates, especially in large organisations.

Pathway submitted narrowly the cheapest of the three bids, but the purchasers ranked their proposal third on eight of eleven technical and management criteria

25 To help them decide which bidder to select, the procurement team ranked the proposals of the three shortlisted bidders in terms of their proposed technical solution and management arrangements. Pathway ranked third against eight of the eleven criteria where a ranking was awarded, including areas where the project later encountered problems such as security against fraud. Pathway's proposals were nevertheless considered deliverable. Their proposal ranked a narrow first in terms of direct price, and a clear first in terms of risk transferred.

A decisive factor in the selection of Pathway was their acceptance of greater risk, making their bid compliant with the Private Finance Initiative

26 The purchasers awarded Pathway the contract despite their ranking on technical and management criteria. Pathway's bid included only £20 million to take on the contractual liability to pay up to £200 million in damages to the purchasers in respect of direct losses if their system failed to operate or to prevent fraud. This was deemed to represent transfer of fraud risk, which was considered essential for the project to qualify as PFI and not count against public sector capital expenditure. The other bidders had priced this liability into their bids pound for pound. The choice the purchasers felt they had was therefore either to accept the Pathway bid or to not proceed with the project at all. The purchasers did not in the end demand damages from Pathway when the project began to slip. They felt this would not encourage Pathway to succeed and could deflect the firm's attention away from delivery to a legal battle. When the Card element of the project was subsequently cancelled in May 1999 the government again chose not to claim damages, as part of the agreement with ICL in which the Company also agreed not to counter-claim. Another major consideration was ensuring the successful completion of the continuing project to achieve post office automation. Currently the platform has been installed in around 8,000 of the 18,300 post offices and is planned to reach the entire network by Spring 2001.

The purchasers found monitoring and controlling risks very difficult

27 During the procurement stage of the project, risk monitoring and control involved mainly discussion between the purchasers' joint procurement team and the bidders about how to mitigate the risks identified in their proposals and demonstrations. By the time that the contract was awarded in May 1996 the register for Pathway still carried six risks that had either high probability or high impact. The procurement team downgraded several major risks because the risk of late delivery was seen as falling on the supplier through the payment terms of the Private Finance contract. In fact, delay, whether caused by a supplier or by a purchaser, would cost the Department of Social Security's business, and therefore the taxpayer, some £15 million each month in terms of continuing fraud and additional administrative costs. It is evident from subsequent events that certain risks the purchasers team had identified in Pathway's proposal and demonstration and declared as cleared in their final risk register for the Pathway proposal in March 1996, remained areas of difficulty. Risks to the timely delivery of the CAPS programme, also identified at that time, were subsequently addressed by the February 1997 re-plan. The key risks are described in Appendix 7 of this report.

Pathway told us that they had not seen the purchasers' risk registers after the award of the contract, and they were surprised that the purchasers had assessed these risks as being high. The Department confirmed that while risk registers were not exchanged, joint discussions around risks were a continuing and regular part of the project management process.

28 After the contract was awarded in May 1996 the purchasers assembled new risk management arrangements by building on the earlier work of the procurement team. The contract was not specific about the reporting obligations of Pathway to the purchasers and vice versa. For example, there was no requirement on Pathway to supply their own risk registers or other internal project management documentation. Reporting took the form of summary presentations and discussion at the Project Board, and further joint planning and progress meetings at working level. The information that the purchasers required for assurance was not defined in the procurement phase or reflected in the management arrangements. Consequently the Department felt under-informed about progress, while Pathway told us that it felt subject to interference.

NAO Conclusions

29 There may be a temptation to think that the Payment Card project failed solely because it was large and complex or because it was a pioneer for the Private Finance route. This is not the case. Various factors contributed to the project's failure and their effects are difficult to disentangle. Looking to the lessons that can be learned by Government, important reasons for the project's failure were:

- divided control. The project was run by two organisations, the Department and Post Office Counters Ltd, with different objectives. Although in theory projects can be run by two or more organisations, in practice this is a recipe for dispute and delay, which is what happened in this case. A key lesson to be learned is that it is usually better to let one purchaser take the lead with proper arrangements for information flow;

- inadequate time for specifying the requirement and piloting. To save time and money, insufficient work went into specifying the project and for demonstrations by bidders. The result of skimping at the start was vast delay and as it turned out, wasted money. A key lesson is that allowing realistic timescales for early planning and detailed specification will pay dividends in time, cost and quality; and

- a shared, open approach to risk management across the whole programme was not achieved. A key lesson learned is that contractual obligations must be underpinned by recognition on all sides of the need for openness about risks identified and emerging.

30 Mistakes of this kind are made time and time again. A Report by the Committee of Public Accounts "Improving the Delivery of Government IT Projects" published in January 2000, shows that government has found learning from and applying its previous experience in project management very difficult. And the Government is not alone in encountering problems with such projects. Questions of culture and training arise – here, as with other projects, those with responsibility too often get immersed in details of procurement and negotiation and lose sight of the effects on the wider business. And if there are fundamental flaws in the design of the management of the whole scheme - as here - the impact of this organisational myopia is compounded. In their report, the Committee of Public Accounts called for the training of more skilled project managers and a high degree of professionalism in the definition, negotiation and management of IT contracts to help address this. And a wider perspective must be maintained. Decisions about IT are crucial to the development and success of the business of public bodies, and cannot be treated in isolation from other aspects of their work.

31 A report by the Cabinet Office in May 2000 has produced recommendations for improving the way in which the government approaches and manages major Information Technology projects. These recommendations are summarised in Appendix 5 and in our view should, had they existed and been implemented in the case of this project, have substantially reduced the risk of it failing to meet the Department's requirements. They may alternatively have led to the project not proceeding in the way it did without changes in terms of its scope and planned timetable. There are lessons to be learned from the project for all three parties involved and for the wider IT community. The Department of Social Security told us that they were seeking to apply the good practice recommended in the Cabinet Office Report, in taking forward their major ACCORD programme to provide new computer systems to underpin their business.

Lessons learned

The lessons learned fall into three main areas; risk management, the procurement of complex Information Technology systems, and procurement by more than one purchaser.

Risk Management

1 For all projects, purchasers should maintain from the start of the procurement stage an assessment of the inherent risk of late delivery, and analyse before signing contracts the sensitivity of their business cases to major slippage and cost overrun.

2 Risks identified should be registered, assessed for impact and probability, assigned to a risk manager and used as a basis for subsequent management and contingency planning. Closed risks should be retained in a closed risk register and reviewed at regular intervals for "re-incarnation". Risk identification must be an ongoing activity, as new risks will occur throughout projects.

3 Departments should appoint a permanent "risk scrutineer", independent of the project team and ad hoc input from consultants, to monitor how the project is handling risks and to report to senior management at regular intervals. This is a feature of the PRINCE 2 project management system widely used in government and in the private sector.

4 Contracts with suppliers, including Private Finance contracts, require detail and clarity about the reporting obligations of suppliers to support risk management and contingency planning by the purchaser. Contractual obligations must be underpinned by a recognition on all sides of the need for openness, extending beyond oral reporting to sharing their risk management documentation.

5 The project illustrates the importance of being able to clarify, quantify and allocate responsibility for risk very clearly if the Private Finance approach is to be a suitable contractual model. In the case of IT development projects in the public sector, this is particularly difficult. Ministers and officials cannot transfer responsibility for the overall service for which they are legally responsible and accountable to Parliament. Some risks, such as the delivery of benefits payments, on which many people depend, are too great for private sector suppliers to absorb and departments therefore must retain a direct interest and involvement in how the service is to be delivered.

6 It is vital that all bidders, and if necessary their parent companies, are clear about the extent of risk transfer proposed by the purchasers at the start of procurement rather than towards the end. Purchasers must ensure that the extent of risk transfer they propose is viable, and must evaluate the extent of risk that they retain. Difficulties in this area can result in the loss of otherwise valid bids.

The procurement of complex IT systems

7 There is often understandable pressure on purchasers and potential suppliers to conclude a deal and to seize as soon as possible the benefits of the project. But it is never acceptable to sign a contract with fundamental “agreements to agree” the detail of the service in the future, even if as in this case, they are intended to be resolved quickly. Allowing realistic timescales for early planning and detailed specification will pay dividends in terms of overall project delivery and cost.

8 Departments undertaking IT procurement projects should fully understand the quality and quantity of resources available which actually will be committed by the supplier to deliver the agreed services. This is particularly important where new software development is required. It should be agreed during the competitive process how resource requirements can be achieved and measured, and the agreement should be drafted into the contract.

9 For major, mission-critical, tailored and bespoke projects, there should be proper piloting of technical solutions to address the full service requirement, rather than reliance on part-functional demonstrations. Departments may have to consider part-funding such pilots and should also consider awarding separate contracts for the design and development of systems before contracting with the developer for full implementation of the successful pilot. This approach also allows keener pricing of the later service implementation and operation stages by suppliers because the risks to them are reduced.

10 There must be agreement between purchasers and suppliers at the outset of information technology projects on the extent to which new systems will either replicate the purchasers’ existing systems, or re-engineer and simplify them.

11 After examining the scope to simplify their business processes, and given certainty as to the detailed requirement, Departments should examine with potential suppliers the scope to use generic and widely used system components where available. This process may in turn suggest modifying the initially proposed solution. A major risk of the Benefits Payment Card elements of the project turned out to be their "bespoke" nature. Building bespoke systems adds to the development costs and the longer-term vulnerability of any solution.

12 Where there are major project developments which involve more than one system being developed in parallel, as was the case here with the Benefit card, CAPS and new Post Office systems, it is sensible to plan and monitor these jointly.

Procurement by more than one purchaser

13 Joint procurement is always difficult, especially where purchasers have divergent objectives. It is better to let one purchaser take the lead with proper arrangements for information flow and reporting to the other. This requires a clear agreement, embodied in the contractual arrangements as well as in a memorandum of understanding, as to roles and responsibilities.

14 Incentives to deliver should pull the same way for both parties to a project: for example, financial and timetable incentives should be mutually supportive: and the parties should agree common objectives and "must-haves" at the outset, as these will influence future behaviour.