

The Inland Revenue proposed PAYE  
computer project. Correspondence with ICL.

Economic  
Policy

PART 1

December 1979

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
<del>25.11.80</del>							
<del>12.12.80</del>							
<del>18.12.80</del>							
<del>19.12.80</del>							
<del>23.11.80</del>							
<del>6.2.81</del>							
<del>9.2.81</del>							
<del>4.2.81</del>							
<del>4.3.81</del>							
<del>1.3.81</del>							
9.3.81							
<del>ends</del>							

PREM 19 / 430

PART

1

ends:-

9. 3. 81

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PART

2

begins:-

10. 3. 81

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SECRET



10 DOWNING STREET

From the Private Secretary

9 March 1981

The Prime Minister held a further meeting this evening to discuss the future of ICL. In addition to your Secretary of State, the Lord President, the Chief Secretary, Mr. Kenneth Baker, Sir Robert Armstrong, Mr. Ibbs and Lord Benson of the Bank of England were present.

Referring to the discussion that had taken place earlier that day, the Prime Minister said she was afraid that the partnership arrangement which ICL were hoping for would fail to materialise. In that case, if the Government were to provide a loan guarantee on the basis proposed in Sir Keith Joseph's minute of 6 March, there would be the all too likely prospect of it having to provide further support in due course. It was partly for this reason that she had asked that the alternative option of providing advance payments on computer purchases and R&D should be considered. In response, Lord Benson said that the partnership prospects were not altogether bleak. Mr. David Scholey of Warburgs had been negotiating over the weekend with NCR, who had expressed interest in a complete takeover of the company. Univac and CDC also seemed seriously interested in buying a stake in the company.

As regards the £100 million guarantee facility that had been proposed, this had not yet been discussed with any of ICL's creditors. The clearing banks had outstanding loan facilities with the company of £112 million, of which about £70 million was firmly committed; these facilities were secured against the company's assets. In addition, other London banks had provided facilities of £50 million and foreign banks £55 million. ICL's cash deficit was forecast to peak at £175 million at end-August. The proposed guarantee was intended to enable the clearers to increase their facilities in the event of the other London banks and the foreign banks withdrawing their support. If the company subsequently failed, the Government would repay them their loans over and above their existing secured facilities.

As regards the option mentioned by the Prime Minister of providing support by way of advance payments, he did not think the amounts would be large enough; and they would not provide a permanent solution.

/The Lord President

SECRET

SUBJECT

File KB  
cc As below  
+ Mr Ingrid



SECRET

- 2 -

The Lord President said that the CCTA were expecting to make payments to ICL in 1980/81 and 1981/82 of about £40 million in total. This amount could, in principle, be advanced to the company now. However, it was unlikely that the company would not have already taken into account the receipt of at least some of this money in the near future; consequently, the benefit to the company of advance payments would be less than on the face of it appeared. Furthermore, there were serious objections of principle to this course: first, the CCTA's contracts would require amendment and this would be criticised by the PAC; and secondly, the pressure on ICL to deliver on time would be considerably reduced. In addition, in so far as it might be said that the Government was providing financial assistance to enable the company to continue trading, the Government might feel bound - because of the implications of Section 332 of the Companies' Act - to meet the company's debts in the event of its being wound up.

In discussion it was generally agreed that the advance payment option was not worth pursuing. As for the guarantee proposal, it was argued that - if the guarantee was to be provided - it should be accompanied by conditions. The objective must be to ensure that a partnership was achieved and that the company should be self-supporting once again. Otherwise, the Government would find itself having to provide further support. It was suggested that one condition should be to ensure that the guaranteed funding should not be used to finance unnecessarily generous redundancy terms for the 5-8,000 employees whom the company were apparently planning to make redundant. If generous redundancy payments were to be made, there was a risk that a potential partner would require a "dowry" from the Government. Secondly, the Government should obtain an assurance that there would be changes in ICL's top management.

In further discussion, it was suggested that it would be unwise to tell the ICL Board that the Government was prepared to provide the guarantee until Ministers were quite clear on the terms and conditions that they wished to attach to it. It should be possible to work out a form of words - to the effect that the Government was looking urgently at the ICL problem - which would persuade them not to call in the Receiver the following day. It was further suggested that the Board should be told that the Government would like Mr. David Scholey to undertake all of the negotiations with potential partners. He should be given a free hand to negotiate the best deal available to the company; for rather than lay down conditions in advance, it would be better for the Government to consider the terms of any partnership arrangement when it had been successfully negotiated and before it was implemented. As for changes in ICL's top management, it was argued that it would be unwise to insist on the Chairman's resignation the following day; he was expected to go, but his immediate resignation might cause more problems than it would solve. Furthermore, it might be wiser not to change the Chief Executive until a new partner was found. In both of these cases, and in respect of other management changes, the Government would be in a position to insist on whatever it wished. But in doing so, it should bear in mind not only the question of timing, but also the fact that confidence in the company would be even more damaged if too many changes were made. Sir William Barlow was mentioned as a possible non-executive Chairman in succession to Mr. Philip Chappell, and Mr. Morgan of GEC as a possible new Chief Executive.

/Summing up,



SECRET

- 3 -

Summing up, the Prime Minister said that they were agreed that the Government should provide the £100 million guarantee proposed by Sir Keith Joseph. But this would have to be on terms and conditions that would minimise the damage to the Government and offer the best prospect of the company finding a partner. Mr. Baker, in consultation with Treasury Ministers, the Attorney General and Lord Benson, should urgently work out the terms and conditions that should be set. In addition, they should prepare a form of words which, while falling short of offering the guarantee, would ensure that the ICL Board did not call in the Receiver the following day. This would give a little longer for the terms and conditions of the guarantee to be finalised.

I am sending copies of this letter to Jim Buckley (Lord President's Office), Terry Mathews (Chief Secretary's Office, H.M. Treasury), Jonathan Hudson (Mr. Baker's Office, Department of Industry), Gerry Spence (CPRS) and David Wright (Cabinet Office).

T. P. LANKESTER

I. K. C. Ellison, Esq.,  
Department of Industry.

SECRET



SUBJECT



cc: Hmt  
Ch. Sec. O.  
Ld Pres. O.  
D01

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10 DOWNING STREET

From the Private Secretary

Co  
9 March 1981

~~CPRS~~

As you know, the Prime Minister held a meeting this morning to discuss the future of ICL. In addition to your Secretary of State, the following were present: Chancellor of the Exchequer, Chancellor of the Duchy, Lord President, Mr. Kenneth Baker, Sir Robert Armstrong, Mr. Ibbs and Mr. Atkinson from your Department. They had before them your Secretary of State's minute of 6 March, the Lord President's minute of 5 March and also Mr. Ibbs' minute of 6 March.

Sir Keith Joseph said that he had concluded, for the reasons set out in his minute, that the Government should provide ICL's clearing bank creditors with a loan guarantee amounting to £100 million. This was the minimum amount that the Bank of England considered necessary to ensure that the banks continued to support the company and to prevent it from going into receivership. The guarantee would require an Affirmative Order under Section 8 of the Industry Act. Its purpose would be to tide ICL over until they were able to complete negotiations for a partnership arrangement with some other company. Mr. Baker added that it was quite clear - and had been for some time - that ICL could not survive without a partner. ICL management had been far too dilatory in seeking a partner. Discussions were now taking place with several companies as indicated in Sir Keith's minute. There had been one further development over the weekend: the US company CDC, had telexed to say that they were very interested in taking a minority stake in ICL's UK business and a majority stake in their overseas business. This would be similar to the proposal put forward by Univac, which had so far looked the most likely prospect.

The Prime Minister said she was appalled that ICL's financial situation had deteriorated so fast without their management apparently being aware of what was happening. If the company were to survive she hoped that their top management would be made publicly to take the blame and be replaced. But she was also dismayed at the lack of financial information on which Ministers were being asked to take a decision. She would have liked to have seen a much fuller analysis of the reasons for ICL's deteriorating position, and it was for this reason that she had asked to see their latest management accounts.

/ The Prime Minister

SECRET



The Prime Minister went on to say that she accepted Sir Keith's conclusion that the company could not be allowed to go into receivership. But she questioned whether as much as £100 million in guarantees was necessary; more importantly, she wondered whether providing guarantees was the best option available. The object must be to avoid receivership at minimal damage to the Government. With the guarantee approach, there would be a risk that no acceptable partnership could be negotiated within the few months breathing space which it would provide; and if this happened, it would then be hard for the Government to disengage. It would also have the disadvantage in terms of publicity, and possible difficulty in Parliament, of involving the Affirmative Resolution procedure. She wondered whether a better approach might be for the Government to make advance payments for purchases and possibly maintenance of computers and to make advance payments on R & D. ICL's other customers might also be asked to help.

In discussion, it was generally agreed that the receivership option had to be ruled out. But it was argued that it was highly undesirable that the issue should have reached Ministers at such a late stage and without more thorough preparation. As regards the advance payment approach mentioned by the Prime Minister, it was suggested that payments of between £50 and £75 million might be possible. But it was doubtful whether this would be sufficient to hold off receivership. In any case, there were also substantial disadvantages in making a cash payment at a time when the public expenditure situation overall was so tight; moreover, there might be problems for the Government from the point of view of its role as a purchaser. This would need to be considered before a decision was taken to go down this route. In addition, whereas advance payments would not be require an Affirmative Order, they would still necessarily become public and they would have to be capable of justification to the PAC.

In conclusion, the Prime Minister said that Ministers would need to reconvene at a further meeting later in the day to which Lord Benson, the Bank of England's adviser on ICL, would be invited. Before that meeting, Departments should urgently examine other options for preventing ICL from going into receivership, and in particular the possibility of advance payments for computers and for R & D.

I am sending a copy of this letter to John Wiggins (Treasury), David Héyhoe (Chancellor of the Duchy's Office), Jim Buckley (Lord President's Office), Jonathan Hudson (Mr. Baker's Office, Department of Industry), David Wright (Cabinet Office) and Gerry Spence (CPRS).

Ian Ellison, Esq.,  
Department of Industry.

*Tim Laker*

**SECRET**



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## ICL MANAGEMENT ACCOUNTS

These are supplied to the Department of Industry under the terms of the 1974 Agreement which governed the payment of £40 million of support to ICL for the development of the 2900 series of computers. Although payments to ICL under the Agreement ceased in 1976, the monitoring arrangements remain in force until the repayment obligation (via a profit formula) lapses in 1983/4.

2 Management accounts in this form normally appear some six weeks after the end of the month in question - ie the printed accounts for January 1981 have not yet been received. However, informal accounting information is available to ICL management far earlier, via the company's own internal computer systems, and it was on this basis that the approach was made to the Department in mid-January to warn of the impending cash crisis and the problems ICL faced in trying to overcome it unaided.

3 The annual budget is normally revised with updated forecasts each quarter. The January revision was the point at which the full extent of the problem was revealed. The December 1980 printed management accounts still show the original budget, though the cash forecast (flagged) is grim.

Department of Industry  
9 March 1981



FUTURE OF ICL: ADVANCE PAYMENTS

(Note by the Civil Service Department)

It was suggested this morning that ICL might be given financial help by means of advance payments for computer equipment and services currently on order for Government Departments.

CCTA expects to pay ICL for equipment and services about £3 million before the end of 1980/81 (that is, almost at once) and a further £23 million before the end of 1981/82. In addition payments for maintenance and hire of equipment (including software licences) amounting to about £13 million will be due in 1981/82.

Thus nearly £40 million could be advanced to the Company from this year's or next year's estimates; these figures have been assessed hurriedly and may not be wholly accurate.

But it is likely that the Company, in making its own financial calculations, will already have taken into account the receipt of the money due this financial year, and in the early part of 1981/82; thus the benefit to the Company of advance payments may be much less than appears.

There are serious objections to this course:

- a. CCTA pays 50% on delivery of equipment and a further 50% on its acceptance; to make these payments ahead of delivery would involve amending the contracts and is likely to be seriously criticised by the Public Accounts Committee.
- b. It would also remove all pressure on ICL to deliver their machines in time; in the past CCTA have found the financial discipline necessary to ensure an adequate service.

The legal implications of this course are set out in the Annex provided by the Treasury Solicitor.

9 March 1981



Given that a pessimistic view is taken of the Company's position, in making advance payments to it, the Government might be regarded as providing it with uncovenanted financial assistance to enable it to continue trading and to obtain further credit from its creditors.

In this case, if the Company were subsequently wound up and the creditors were not met in full, the Government might be prejudiced by the application by analogy of Section 332 of the Companies Act 1948. The Law Officers have advised that the Crown should behave as if it were bound by this Section although this is not strictly so.

At worst, this would mean that the Government might have to meet the Company's creditors in full. To avoid this difficulty, it is desirable to give assistance in these circumstances only if it is reasonably clear that by virtue of it the Company will be enabled to continue trading with a reasonable prospect of meeting its creditors in full. This would be the case either if the advance payments would in themselves tide the Company over a temporary cash flow problem, or if they were designed to cover the position temporarily until the result of an approach to its bankers was known.



Mr. Lamberton,

CHEQUERS  
BUTLER'S CROSS · AYLESBURY  
BUCKS

Coming Mon am.  
Information requested  
from DoI  
5/1  
8/3/8

Mr. Clerk

I.C.H.

~~Copy this note  
to Sir J. Sir R.A.  
Sir H. Mr.~~

We require in time for to-morrow's  
meeting, the last 3 separate quarterly  
management accounts.

And preferably the last 6 separate  
monthly management accounts.

DoI should have these - otherwise  
it is difficult to imagine how they can  
be recommending a guarantee of the size  
proposed.

N.B. Being a Computer and Systems  
Company, the doc should not  
only be detailed but up-to-date;



£45 £24 £35m

# ICL LIMITED

## Statement by the Chairman, Mr. E. P. Chappell, C.B.E., at the Annual General Meeting held in London on 3rd February 1981.

Last December, we announced our results for the year to 30th September 1980. They revealed a sharp drop in profit in the second half of that year, as well as the expectation that adverse trading conditions would continue well into the current year.

These trading conditions have certainly not abated in the first quarter. In its overseas markets ICL is still faced with the problem of the continued strength of sterling; and the economic scene in our principal market, the U.K., has deteriorated to such an extent that Britain is now in far deeper recession than the other major industrial countries.

Such circumstances mean that regretfully the ICL Group is currently trading at a loss. Due to phasing of deliveries, profitability in our first quarter in any year is usually low and indeed the first quarter of the current year was budgeted to be a loss. A particularly low volume of despatches has caused the loss to exceed budget and our unaudited management accounts show a Group pretax loss in excess of £20 million for the first quarter. Substantial measures have been taken to reduce costs and to increase deliveries, and I must emphasise that this is not the running rate of loss for the year.

In the present economic climate it would be imprudent to attempt a detailed forecast, but given no further deterioration in demand and maintained confidence in the present excellence of your Company's products, we would expect to reduce the loss rate in the second quarter. In the second half of the year we plan to achieve an overall result approaching break-even, so that the loss for the full year will be restricted to about the same level as that of the half year.

The outcome for the ensuing year 1981/82 is difficult to predict. In our business, a relatively small down-turn in orders means a sharp reverse in profitability; equally, a relatively small up-turn in demand can bring with it a sharp improvement. Therefore, given a revival in worldwide markets, and especially in the U.K. market, we would expect a significant improvement in the profitability of our operations.

So far as funding is concerned, it is normal for us to have a cash outflow in the first quarter of each year; but management action to conserve cash resources has meant that the increase in our borrowings in the first quarter of the current year was no more than in the equivalent period last year. We have considerable unused facilities available at present from our bankers. In this connection, our principal bankers have been kept fully informed as a matter of course about our trading position and future plans.

Our order-take in the first quarter showed a modest improvement for our overseas business compared with last year; our total orders received overall for the first quarter were, in fact, ahead of last year, but a slightly higher proportion than normal of those orders in the U.K. is for delivery in later years.

We have taken and are still taking very determined actions to reduce our overall costs :-

**Cash** In present conditions, the control and conservation of cash is our first priority. Our drive to reduce demands on working capital is being fully maintained and intensified wherever possible. Expenditure in all parts of the Group is subject to rigorous control.

**People** We have already announced our proposal last November to reduce our manpower by 2,500 people, and this is now being implemented. Those elements of the total costs which relate to the closure of the Winsford factory will be treated as an extraordinary item in our 1981 accounts.

**Pay** The 1981 annual pay negotiations in ICL began in January with the hourly-paid employees. ICL has responded to their claim by stating that we cannot afford a general increase in pay during 1981.

**Production** We are continually reviewing our manufacturing programme in the light of our trading position.

**Premises** Since the middle of 1980 we have, in the U.K. alone, disposed of or contracted to dispose of almost 14 per cent. of our total U.K. spaceholding. Further premises disposals are being considered.

The other main element of our present policy is to sustain as far as possible the levels of investment in the key areas of our business, so that we can remain competitive and be in a position to respond

Cash - £100m Aug 1/80.



when demand resumes. This will bring benefit to our shareholders, our customers and our employees and, we believe, to the nation. We therefore look to our shareholders, our customers and our employees to express their confidence in ICL by supporting us fully in carrying through the policy I have outlined.

Recent Press comment has linked ICL with companies in the oil industry; ICL has had no such discussions. It has also been suggested that ICL has asked H.M. Government for financial support. We do of course maintain very close relations with the Department of Industry. They are fully aware of the difficult short-term problems facing us and of our plans to surmount them.

In difficult times we rely on the strengths of the Company and it would be as well for me to reiterate the more important of these:—

**Turnover** We have succeeded in growing our turnover at over 18 per cent. per annum over the last decade. This has been done through volume increase with little or no price inflation and against strenuous competition.

**Overseas** Our business overseas has also increased consistently, and in 1980 overseas turnover exceeded £300 million for the first time. Not many businesses have grown their overseas turnover from £46 million to £312 million in a decade.

**R & D Spend** We have been increasing our research and development expenditure at a rate of nearly 20 per cent. per annum.

**Product Range** Our whole product range has been fundamentally changed during the 1970s. We have successfully accomplished the transition from the 1900 Series to the 2900 Series with its modern architecture designed to cope with customers' needs in the ever-changing world of computing. We are proud of the scale and quality of that achievement.

We have recently introduced some outstandingly successful new products including the ME29, the 2955 and the 2966. Over 750 orders for the ME29 have now been taken. There are more excellent new products in the pipeline, of both an enhancement and an innovative nature, with particular emphasis on mini-computer products.

Our operating software is mature; it has become accepted as highly versatile, efficient and cost-effective. Our Information Processing Architecture is recognised as a very effective means of providing our business users with the best flow of information needed to run their businesses efficiently.

We have never before had such a competitive range of products. This product excellence has come at a time of economic recession. But it enables us to offer hard-pressed businesses a most effective means of control and of being able to react swiftly to the changing environment.

**Customer Base** The value of ICL's customer base is well over £2,000 million in 80 countries. Apart from our largest rival, we have the biggest customer base outside America and Japan of any computer manufacturer.

**Services** We have increased our business in software and other computer-based services very considerably in recent years. In Dataskil we possess one of the largest software houses in Europe. We also have a worldwide reputation for producing applications software which will stand up to competition anywhere. We have extensive international computing bureau operations and education and training facilities. The whole services business is a fast-growing element of the information technology industry, and ICL is well placed to succeed in this highly important market of the future.

**Employees** ICL has highly-skilled, dedicated and very hard-working employees throughout its business. In them we possess skills, experience and loyalty which are second to none.

ICL has real assets: an excellent product range, a sound and extensive customer base, and our employees. The market for our products will revive as the U.K. and world economies recover. With that revival will come fresh opportunities for ICL's business to grow profitably. Your Board is determined that ICL will play a leading part in the dynamic growth of the information processing industry.





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cc Mr Duguid  
Mr Wolfson.

PRIME MINISTER

FUTURE OF ICL

Since Kenneth Baker reported to you on 6 February, the banks (led by the Bank of England) have finished investigating ICL's financial position and prospects. ICL's senior management have discussed possible partnership with four overseas companies.

RECENT DEVELOPMENTS

2 None of the companies approached have expressed interest in an outright bid. Two US multinationals (Univac and CDC) seem genuinely interested in the prospect of a major stake in ICL and have followed up initial contacts quickly. The initial reaction of the Japanese (Fujitsu) has been disappointing, but exploratory discussions continue. There has also been preliminary contact with St Gobain. NCR, which has not been approached by ICL, has also expressed interest. ICL management seem to have entered into the discussions whole-heartedly and to have overcome their earlier reluctance to contemplate the loss of their independence.

3 It is clear that all prospective partners are approaching a possible deal cautiously; they will need time to assess both the cost of investing in ICL and the practical and financial implications of subsequent rationalisation. Negotiations on





partnership seem likely to take three to six months (but Heads of Agreement might be achieved on a shorter timescale).

4 ICL's financial situation has continued to deteriorate. Although the banks' investigations have not revealed any new factors which would call in question the earlier forecasts of loss and overdraft, the level of new orders which will produce revenue in the current company year has been falling below forecast. The main reason for this is uncertainty about the company's future, which causes prospective customers to hold off from commitments. As a result, the loss for the year to end September could now be £50 million rather than £35 million, reducing net worth in the new balance sheet to as little as £80 million (currently £141 million) and with total borrowings of £240 million.

5 The Bank of England considers that the clearing banks are on the point of deciding that in this situation they cannot prudently stay with the company. Their current exposure is about £20 million and they believe they could recover this in a liquidation. If they stay with ICL, their exposure is expected to grow rapidly as ICL moves towards the forecast peak overdraft levels in May and August (around £175 million). In addition, if any of ICL's other borrowing facilities (£120 million divided between UK and overseas' sources) are withdrawn, ICL would need to seek to increase its drawings from the clearers in order to offset this reduction.





6 The ICL Board are monitoring very carefully their position under Section 332 of the Companies Act. As the attached letter from the Chairman (Annex A) makes clear, the Directors will consider at the Board meeting on 10 March whether to cease trading, if there is no indication that support is available to tide them over until the partnership discussions are completed.

#### THE OPTIONS BEFORE US

7 The Government needs to decide its attitude to ICL's future. There are only two options: do nothing thereby letting ICL go into receivership, or to participate in temporary support measures to get the company through its immediate difficulties until a partnership is established.

8 My first inclination is to favour receivership; that is the appropriate market response and it could be expected that others would be willing to acquire the profitable parts of ICL's business. I am satisfied, however, that receivership would be destructive and expensive to the taxpayer. The Bank of England have concluded that the special nature of ICL's trading would make it most unlikely that much of value could be saved from the rump of the business. Receivership would involve the break-up of the company despite the fact that it has a credible product range (there is evidence that, even in the current recession, ICL would be making significant sales if its stability as a company was assured). Receivership





would also dissipate the customer base, which is ICL's main attraction to any potential partner. The expense arises because users, especially Government users, would incur the heavy conversion and transfer costs mentioned in the Lord President's minute of 9 February and there is a risk of them being unable to secure even basic maintenance. Also there would be no way of recovering more than a fraction of ECGD's current exposure on ICL's business (about £120 million).

9 Receivership would in addition affect a number of overseas customers (notably the EEC, the European Space Agency and the Abu Dhabi National Oil Corporation) and many public and private sector organisations in the UK which either supply ICL or which rely on ICL equipment to provide services to others. Damage would be done to the United Kingdom's international reputation in the supply of major equipment. (A note of the main Government operations relying on ICL computers is at Annex B.)

10 Three considerations appear to justify Government participating in temporary support measures. As users, we have an interest in the company's future; until the end of last year we gave preference to ICL in major public sector computer contracts and central Government remains the single biggest user of ICL computers. The survival of ICL will help protect the significant investment we have made. Our policy on information technology seeks to persuade manufacturers, users and backers to make significant investments in new and untried technologies; many of those





concerned will judge the seriousness of our intentions by our treatment of ICL in the current crisis. As previous shareholders in the company, we have something of a moral commitment; the NEB disposed of its shares in December 1979 at a profit of £25 million on its investment and, if a merchant bank had done the same, current developments might well make it feel obliged to repurchase the shares. We could not in any circumstances escape criticism for selling our shares so soon before a collapse (even though the collapse is entirely unexpected).

11 We cannot ignore public sentiment. I do not recommend that we should support ICL for reasons of national prestige; Concorde and Rolls Royce provide sufficient warnings. But we must remember that ICL is seen at home and abroad as a significant national asset in which all can take pride; receivership would be a blow to public morale. On the other hand assistance to ICL, following on the heels of our assistance to BL, British Steel and the NCB, would be seen as evidence of a weakening of our resolve not to rescue lame ducks. A decision to aid ICL might be widely misunderstood.

12 Against this background I consider that on balance we should join the banks in providing ICL with sufficient support to prevent its collapse and to see the company through to partnership with a major company. I do not make this recommendation lightly and I would intend our support to be the minimum consistent with ICL's survival, for the shortest practicable period, in a form





which imposed the least burden on public expenditure and to be given in a way which appeared to minimise the Government's role while maximising that of the banks.

13 The Bank of England have advised that we might best assist by providing the clearing banks with a guarantee to cover any potential additional exposure that might result from a loss of confidence in the company by uncommitted lenders before a partnership deal was concluded. I am advised that an "identified term loan facility" of £100 million might meet this requirement and I have powers to offer such a guarantee under Section 8 of the Industry Act. I am normally advised on the use of these powers by the Department of Industry's Industrial Development Advisory Board (IDAB) and the offer, which could only be made after an Affirmative Resolution, would have to be approved by the European Commission.

14 The merit of a guarantee is that the expenditure would fall on the banks and there would be no cost to the Exchequer except in the event of the guarantee being called (which would not occur for some time). Presentationally a guarantee is clearly preferable to direct financial assistance since the Government would not be in the lead. In order to further minimise the Government's apparent role, I intend to approach a few major users of ICL equipment, and some of ICL's suppliers, all of whom stand to lose from a receivership, to see if they would join in offering





support; if they agree our role would be reduced to being one in a "club" of supporters.

15 A decision to assist ICL would also have to be presented carefully to avoid any implication that the aim was simply to buy time for negotiating a partnership. Any such hint would cause ICL's prospective customers to cease ordering until a partnership was in place, which could precipitate the financial collapse we seek to avoid. On the other hand, properly presented, the announcement of support would engender confidence and reduce the risk that a guarantee would be called in practice.

16 The Department and the Bank of England agree that our support would have to be accompanied by immediate changes at ICL, certainly involving the Chairman and possibly also the Managing Director.

17 If we extend a guarantee I believe we would be well placed to ensure that ICL's negotiations for a partnership reach an outcome which meets our interests. Under the terms of the support given to ICL in 1972/76 for the 2900 series of computers, I have responsibility for judging whether a foreign partnership would assure "the maintenance and further development of a capability in the computer systems industry" in this country. I have the right to reclaim £40 million paid earlier to ICL, with interest, (now some £70 million in total) if I am not satisfied. This would give the chance to influence the future level and direction of





R & D work undertaken by the partnership so as to ensure that current Government users of ICL computers obtain either continuity of development or an orderly and economic transition to another manufacturer's machines. I would also expect to continue support for worthwhile ICL projects under existing legislative arrangements and within existing financial provisions. I would hope that any partnership package would include an agreement for continued R & D support for major new projects identified by ICL.

18 I therefore recommend that we should agree in principle to extend a guarantee to ICL's bankers on the lines I have described. Precise details will need to be settled with the Treasury and the Lord President will need to be kept in close touch with developments. Immediate steps will need to be taken to inform the Bank of England so that it in turn can take the necessary steps to prevent the Board of ICL taking any irrevocable action at its meeting on 10 March. I shall also need to obtain formal advice from IDAB which is also meeting on 10 March. Early steps will need to be taken to make a public announcement and to consider how we should approach the House to obtain approval for the guarantee, but the precise steps will need careful preparation in view of the twin risks of damage to ICL's prospects of survival and of criticism from our supporters.

19 I am copying this minute to the Chancellor of the Exchequer, the Lord President, the Chancellor of the Duchy, the Chief Secretary,





9

CONFIDENTIAL  
COMMERCIAL IN CONFIDENCE

the Minister of State in the Civil Service Department,  
Sir Robert Armstrong.

14

K J  
6 March 1981



ICL Public Limited Company

From the Chairman  
E P Chappell CBE



ANNEX A  
ICL House, Putney, London SW15 1SW  
Telephone 01-788 7272  
Telex 22971

Sir Peter Carey, KCB  
Permanent Secretary,  
Department of Industry,  
Ashdown House,  
123 Victoria Street,  
London SW1E 6RB



Commercial in Confidence

5th March, 1981

*Mr Lurgan: for advice  
& draft reply asap  
please*

*Dear Permanent Secretary*

*cc Mr Croft  
Mr Atkinson*

Our various discussions over the latter half of 1980 and, more particularly, the two proposals we made to you in January and February of this year, will have made your Department fully aware of the severe effect that the deterioration in our business environment in the latter half of 1980 and so far this year has had on ICL's business. In financial terms, our present forecasts indicate that by 30th September, 1981, shareholders' funds will be reduced to about £80 million and total borrowings will increase to about £240 million (including ECGD Finance of £104 million). We have a peak bank borrowing position in August, 1981 of £175 million. Our fully committed bank facilities in August would, on present assessments, amount to only £110 million: and, in any event, projected borrowing figures are unacceptably high in relation to shareholders' funds.

As you are already aware, the Board has already concluded that it was not practical to envisage ICL continuing alone and that the creation of a new partnership arrangement (of a pattern to be agreed) was essential to long-term survival and could offer major potential benefits. We are aware that approaches had been made by you to certain U.K. companies without success. The Board has also carefully assessed which overseas companies might be most interested in ICL and discussions are already in progress with five overseas companies namely, in alphabetical order, Control Data Corporation, Fujitsu, NCR, Saint-Gobain and Sperry.

It has always been understood between us that a period of some months may well be required if any of these discussions are to be transformed first into serious negotiations and then for the negotiations to be completed. There are other potential partners who might have an interest in ICL to whom approaches would be made subsequently if circumstances permit.

Continued



The evident deterioration in ICL's financial position is also now a cause of increasing concern, both to its bankers and to existing and potential customers. It is above all true in the computer industry that customers need to be convinced that following the purchase of equipment they will receive the continued long-term support from the provision of hardware enhancements, software and proper service and maintenance implied or expressed in the supplier's commitment to the customer. At the moment our order position, and consequent revenue, is being adversely affected by continuing uncertainty and a reassuring public statement is needed.

Intensive discussions, under the co-ordinating role of the Bank of England, have been held with ICL's principal U.K. banks who have been asked whether they would substantially increase the bank facilities which they make available to ICL. These banks have not felt able to give an assurance of the increased facilities which appear necessary to enable the Company to continue to trade pending the completion of the negotiations. Cash flow projections suggest that existing facilities will only meet cash requirements up to May at best and, at worst, would be exhausted by early April.

Consideration has been given to the possibility of obtaining additional funds from our shareholders and the two largest, the Post Office Pension Fund and the Prudential, are being approached. ICL's financial advisers, Morgan Grenfell and S.G. Warburg have advised the Company that shareholders, however, will not be able to provide funds on the scale and within the time required. Our financial advisers have discussed with your Department the possibility of obtaining support from major users: this route would require positive commitment and leadership from HMG, being by far and away the largest user.

Following your discussions yesterday with Lord Benson, Mr. Mackworth-Young and Mr. Scholey, you will be aware that the executive Directors of ICL have concluded that in these circumstances, unless they are satisfied that sufficient additional facilities will be committed quickly so that a reassuring public statement can be made, there seems no alternative but to request the appointment of a receiver: and this will be considered at a Board meeting on Tuesday, 10th March.

ICL and its financial advisers have concluded that in the timescale available Her Majesty's Government is the only practical source of the necessary financial support which will enable these needs to be met so that the Company can continue trading and the partnership discussions can be continued.

*Your sincerely*

*Philip Chappell*

E P Chappell



ANNEX B

THE DEPENDENCY OF GOVERNMENT OPERATIONS ON ICL COMPUTERS

Because the policy of successive Governments has been to procure predominantly ICL computers there is now a heavy dependence on their continuing operation in order to maintain large scale administrative tasks in Government. The following examples illustrate the breadth and scale of these operations.

CUSTOMS AND EXCISE DEPARTMENT

The processing of VAT receipts average some £45m per day.

PAYMASTER GENERAL'S OFFICE

Acts as clearing bank for all Government payable orders and pays public service pensions.

DEPARTMENT OF NATIONAL SAVINGS

The National Savings Bank; Premium Bonds; Government Stocks; and National Savings Certificates, all of which contribute to Government funding.

DVLC

This handles the issue of driver and vehicle licences, as well as providing a direct service to the police.

MINISTRY OF DEFENCE

The department relies heavily on ICL machines for a wide variety of operations including stores and supplies to the armed forces, intelligence and security work, payment of suppliers' bills, and scientific tasks.

DHSS

The handling of unemployment benefits; pensions records and payments; and various Social Security benefits.

MAFF

Grants and subsidy payments including import/export levies as required by the EEC.

INLAND REVENUE

PAYE assessment (for Scotland), PAYE collection, Corporation Tax assessment and collection.



cc A Wignall

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COMMERCIAL - IN CONFIDENCE

Qa 05274

To: MR LANKESTER

From: J R IBBS

Future of ICL

1. In his minute to the Prime Minister, the Secretary of State for Industry explains why, in the special circumstances of ICL, there is a case for the Government to buy time for the company by guaranteeing £100m. of its borrowings rather than to allow the company to go into an immediate receivership. The only commercial justification for providing this guarantee is that it gives the company time to secure a reasonable partnership with another computer manufacturer.

2. On balance we believe the Secretary of State is right in recommending that the company should be prevented from going into immediate receivership. The grounds for this are:

- that, because of its heavy dependence on ICL equipment, the public sector is extremely vulnerable to a major disruption of essential business if receivership occurs;
- that if we are to be taken seriously as an international force in Information Technology, we must preserve a substantial home-based computer manufacturing capacity;
- that, with a receivership, there would be no certainty that such a capacity would be retained.

3. We must point out that there is a risk that any attempt to prevent receivership may lead to a greater liability than the guarantee of £100m. There is some possibility, which has to be accepted, that no acceptable partnership could be negotiated by the end of the few months' breathing space and that we shall again be faced with a choice between receivership and a further guarantee. Moreover, once it has embarked on support, the Government may find it difficult to disengage without meeting obligations going wider than its immediate guarantee (even if the guarantee itself is carefully worded to avoid this).



CONFIDENTIAL  
COMMERCIAL - IN CONFIDENCE

4. If a partnership is to be the outcome, it is important that the choice of partner and the terms of partnership should be as satisfactory as possible from the Government's point of view. To ensure this, it may well be necessary for the Government to give clear guidance to ICL.

5. The best partnership from the Government's point of view might not necessarily be the most attractive to ICL. The Department of Industry has prepared its list of desirable criteria, and the CPRS urges that this should be used in guiding ICL towards an appropriate partner. Fortunately, the Government should have some leverage on the choice of partner through its right to withdraw the £70m. of development support mentioned in paragraph 17 of the Secretary of State's minute.

6. In the CPRS's view an important characteristic of a partner would be that it should have a secure future in its own right as a computer manufacturer and should be willing to retain a substantial manufacturing capability in the UK and source components from there. In the case of some of the prospective partners, we have doubts on these points.

7. I am sending a copy of this minute to the Private Secretaries to the Secretary of State for Industry, the Chancellor of the Exchequer, the Lord President, the Chancellor of the Duchy of Lancaster, the Chief Secretary, the Minister of State in the Civil Service Department, and to Sir Robert Armstrong.



6 March 1981



Ref: A04409

PRIME MINISTERFuture of ICL

At your meeting at 11.15 am on Monday 9 March you are to discuss the minutes to you of 6 March from the Secretary of State for Industry and of 5 March from the Lord President of the Council. The Chancellor of the Exchequer, the Chancellor of the Duchy of Lancaster, Mr Kenneth Baker and Mr Ibbs will also be attending.

2. The immediate issue is set out in paragraphs 5 and 6 of the Secretary of State for Industry's minute. The Bank of England - Lord Benson is leading for them on this - judge that the clearing banks are on the point of withdrawing support from the company: their exposure is likely to rise from £20 million currently to peaks of £175 million in May and August. The ICL Board will meet on 10 March to consider their position under Section 332 of the Companies Act and whether to appoint a receiver, if by then there is no indication that support is available to tide them over until their discussions with prospective partners are completed - see, in particular, the last two paragraphs of the letter of 5 March from the Chairman of the Company which is annexed to the Secretary of State's minute.

3. The main case for Government action to avert collapse and break up of the Company rests on the fact that public sector bodies are major customers, dependent on ICL for maintenance of systems and for new systems now on order. Quite apart from the 200 ICL computers in Central Government, the National Health Service, the nationalised industries and the local authorities are all major users. The problems are set out more fully in the minute to you of 9 February from the Lord President, in the letter from DHSS to Mr Lankester of 3 February and in Annex B of the Secretary of State for Industry's present minute. The Lord President has estimated that conversion costs alone could cost Central Government £150-200 million quite apart from the costs of delays in new systems and of maintenance problems.

4. The other main reasons why it is in the Government's interests to avoid disorderly collapse of ICL are -

- i. overseas users, who were encouraged by the Government to buy from ICL, would also be hit at cost to the general reputation of United Kingdom exporters;



ii. failure to support ICL could undermine current efforts to promote information technology (paragraph 10 of the Secretary of State's minute of 5 March);

iii. when the NEB sold their shareholding in December 1979 the price was equivalent to 120p compared with 39p today and those who bought the shares could well be critical of the Government if it now stood back.

5. Against this background the Secretary of State for Industry reluctantly recommends (his paragraph 13) that the Government should guarantee an "identified term loan facility" of £100 million by the clearing banks. In effect this would be a Government guaranteed bridging loan available until a long term partnership could be negotiated. It would be designed to make clear that the Government's guarantee was limited to a specific loan facility and did not extend to underwriting the liabilities of the company as a whole. It would be given under Section 8 of the Industry Act and, therefore, would need to be preceded by the formal advice of the Industrial Development Advisory Board, an Affirmative Resolution, and the approval of the European Commission. No public expenditure would be involved unless the guarantee, or part of it, were called. It is possible that the amount for which the Government was obligated could be reduced if other major customers and suppliers could be persuaded to join the Government in making the guarantee (paragraph 14 of the minute).

6. In return for the guarantee the intention would be to ensure -

i. the replacement of the Chairman and possibly the Managing Director (paragraph 16);

ii. a positive role for the Government in ensuring that ICL's negotiations for a partnership recognised the public sector's interest as customer (paragraph 17).

Paragraphs 2 and 3 explain that so far there has not been any substantial progress in negotiations for partnership and that it would take from three to six months to clinch a deal.

7. The Lord President of the Council strongly advises in his minute of 5 March that, to avoid a collapse of many of the Government's computer systems, the Secretary of State's proposals should be accepted. He warns, however, that it will now be necessary to look very carefully at any proposals to place new orders with ICL.



8. Since the Government would not be taking a stake in the ownership of the company or itself lending the company money, and the guarantee would be made under existing legislation, I think that you could justify the proposed guarantee in relation to what you said to Brian Walden in your Weekend World interview on 1 February (see the attached extract from the transcript). But I suppose we cannot exclude the possibility that part of the price of any partnership deal will be that the new owner should be relieved of some part of ICL's liability.

## HANDLING

9. After the Secretary of State for Industry has introduced his paper you will wish to hear the advice of the Lord President of the Council who is, in effect, representing the public sector customers. The Chancellor of the Exchequer will want to comment on the financial aspects and the Chancellor of the Duchy of Lancaster on the timing and tactics of the Affirmative Resolution.

10. If you accept that it is essential to avoid the costs and disruption to public sector services of an abrupt break up of ICL, you will then wish to consider what action the Government should take. It might be argued that receivership could be justified on the grounds that the receiver might well be able to safeguard the interests of customers and, moreover, would wish to do so in the longer term interests of the company. The Secretary of State for Industry, however, advises in his paragraph 8 that receivership would lead to the break up of the company; and this appears to be the view of the Bank of England too. You might well conclude, therefore, that while receivership might preserve customer interests, it is just not worth the risk.

11. If so, you will wish to turn to the proposals for the guaranteed loan in paragraph 13. A possible difficulty is that it should not be taken for granted that the clearing banks will co-operate by making the proposed loan facility available, even under guarantee. Their attitude might be influenced by the Budget. If you decide in principle that the Government should be willing to give some bridging support, it will be prudent, therefore, not to rule out the need to look at alternative methods if necessary.



12. You will also wish to decide whether you want the Secretary of State for Industry to pursue the idea in his paragraph 14 of involving other major customers and suppliers in the guarantee. While this is attractive in principle, you will wish to be satisfied that it would not run the risk of leaks which would further sap customer confidence.

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#### CONCLUSIONS

13. In the light of the discussion you will wish to give the Secretary of State for Industry authority for the action which he may take before the ICL Board meeting on 10 March. If the proposed guarantee of a bridging loan is acceptable, you will wish to record any qualifications to the Secretary of State's approach and, perhaps, to leave open the possibility that the proposal might have to be modified in the light of the clearing banks' reactions. You will also wish to reach a provisional view on the timing of the Affirmative Resolution although this will turn in part on the outcome of the Board meeting and of the banks' reaction to the proposals.

14. Finally you may wish to ask the Secretary of State for Industry to inform the Cabinet or the Ministerial Committee on Economic Strategy, in a brief oral statement, on 12 March of the position then reached.

REA

ROBERT ARMSTRONG

6 March 1981



expand in those areas there shall be help for them. You've already got a budget for that, that's what I mean by selective help. Let me give you an example .....

BRIAN WALDEN:

What about Talbot or ICL then? Supposing they come along, are you going to give them selective help?

MARGARET THATCHER MP:

If they're slap right in the Midlands or if they're slap right in a non-development area, they do not qualify under existing legislation.

BRIAN WALDEN:

And they won't get it?

MARGARET THATCHER MP:

And they won't get it. If in fact they're in the development areas they already qualify for help ....

BRIAN WALDEN:

Of course.

MARGARET THATCHER MP:

under existing legislation. Just let me give you an example. I also was very worried about Bowaters when they put newsprint right out. Now there were things that we could have done and that we offered to do, well within Government and nationalised industries power to help, well within the legislation. One of the things was that if they expanded there and really modernised they would have got help under existing Industry Acts within existing budgets. Now this is why I'm making it clear, some people say well that was government help. It was help in fact, under existing budgets,



Well, I'm trying always, as you know, to be candid with you  
but honestly these decisions are very, very difficult.

BRIAN WALDEN:

I know that. But I smell something of real importance there.  
You said you never want to take on anything like Leyland  
again...

MARGARET THATCHER MP:

No, I don't

BRIAN WALDEN:

So can you firmly pledge that ICL, Talbot, anybody else who  
comes along with the begging bowl, you're not in fact going  
to put a lot of money into it.

MARGARET THATCHER MP:

I'm not going to take on, as British Leyland was taken on,  
another.....you see we're 95% owner of British Leyland.

I just can't take that on....

BRIAN WALDEN:

And you're not going to do that again?

MARGARET THATCHER MP:

No, no, no we've done it and I just, we can help sometimes,  
you can do selective help, but never, never, never take on  
the ownership.

BRIAN WALDEN:

Ah, I'm a bit worried about selective help. How much does  
selective help cost as opposed to what Leyland has cost?

MARGARET THATCHER MP:

Well I think you're reading more into what I'm saying than  
I intend. You've got companies in the development areas.



SECRET

laa

✓ Mr Hodgson  
✓ Mr Wilson



From for  
Monday 16.15

PRIME MINISTER

ICL

I gather that there is a strong chance of ICL going into Receivership on Tuesday if the Government takes no action. We are going to discuss Sir Keith Joseph's proposals for support on Monday.

I drew attention to our vital dependence on ICL in my minute to you of 9 February. By far the most important part of this is the need to keep our present machines going. If the Company goes into Receivership there is no certainty that this will be possible; at best there is likely to be a break in maintenance cover, and this could mean some machines stopping work within hours, and almost all within days. My colleagues will be best able to judge what effect this would have on their operations.

I am driven unwillingly but remorselessly to the conclusion that it is essential to prevent the Company from collapse in order to avoid this situation, and therefore hope colleagues will support Keith Joseph's proposal to do so. Even so, uncertainties about the nature of the future partnership, which it is still vital for the Company to seek, will make it necessary to look very carefully at any proposals to place new orders.

I am copying this to Geoffrey Howe, Keith Joseph, Francis Pym, Kenneth Baker and to Sir Robert Armstrong.

S.

SOAMES

5 March 1981

SECRET



Mr Whitmore <sup>la</sup>

Sir R. Armstrong. (over)

E 0208

MR NEAIGHT  
*Spw*cc: Mr Ibbs  
Mr Le Cheminant

You will wish to discuss urgently with Mr. Whitmore. In view of the sensitivity of the issue, it may be thought better to go for a small meeting, rather than E, with Sir K. Joseph notifying the Prime Minister. The question of fraudulent trading arises from the Companies Act: continuing to trade without obligations being covered. Mr. Lancaster has a copy of this.

ICL: E Committee  
*Spw*

The Secretary of State for Industry wishes the Ministerial Committee on Economic Strategy to discuss ICL on Monday 9 March. <sup>5/3.</sup>

Following a meeting between ICL, their banks and the Bank of England on Tuesday the Finance Director of ICL and at least one of the non-executive directors are apparently talking in terms of fraudulent trading and, therefore, the need to go urgently into receivership. The next meeting with the banks and the Bank is on Tuesday 10 March - hence the need for a meeting on 9 March to establish the Government's line.

The Secretary of State for Industry will circulate tomorrow morning a memorandum - probably jointly with the Lord President of the Council - seeking authority for a Government guarantee of some bank lending to ICL pending further studies and work on possible collaborative deals. This would be given under Section 8 of the Industry Act and would require Affirmative Resolution. It would be presented in terms of the Government acting in its role of a principal customer concerned to protect its own services.

If it is agreed to hold a meeting of E as proposed I recommend that, in view of the Budget on the following day, the Chancellor of the Exchequer should, if he wishes, be allowed to ask the Chief Secretary to act for him. In view of the need to preserve strict commercial confidentiality, and to ease the task of setting up a large meeting quickly, an alternative would be a meeting



confined to the Prime Minister, a Treasury Minister, the Secretary of State for Industry, the Lord President, and, probably, the Chancellor of the Duchy. Either way, the Secretary of State for Industry would wish to bring Mr Kenneth Baker with him.

DJM.

D J L MOORE

5 March 1981

~~See above briefing.~~

5 agree.

the Comm. Minis to ed held - meeting

on Monday at 1530 or 1600.

Make or run it with the app comm / 12?

Mr Whitby

Clearly we must have a meeting.

AKS  
5 iii

I think it should not be a full E,  
in view of commercial sensitivity, but an  
ad hoc meeting is done.

~~AKS~~ 5 iii



5 March 1981

MR LANKESTER

I am invited to the ICL discussion at 4.15pm on Monday. In fact, I don't think it is necessary for me to be present. I have no special knowledge of the ICL situation beyond what I passed to the Prime Minister in my note last night. And the problem is one of business judgment and industrial policy rather than IT products and markets.

I propose to work at home (in Suffolk) on a first shot at the Central Council speech, which Ronnie and I are due to talk to the Prime Minister about on Friday, 13 March.

X I would like a copy of any papers from CPRS,  
Robert Armstrong, DoI on ICL.

both wrote a  
6/3.

JOHN BOSEYNS



4 March 1981

Policy Unit

*Tim*

*Clin. to see  
4:30  
TL*

*Ecan Pol*

*original referred to J.H.*

PRIME MINISTER

ICL

Ken Baker rang me today to give me advanced warning of ICL developments. The position is as follows:

1. There are three potential bidders, in order of likelihood and suitability: Sperry Univac, Control Data Corporation, Fujitsu.
2. ICL Directors are a bit jittery, have been taking advice about their personal positions. There is a lack of confidence in the City for obvious reasons.
3. Total overdrafts are about £110m, but only about £10m of this is with the home clearers. The main exposure of £100m is overseas and ranks lower down in the debt queue.
4. The clearers would help with financial support provided there are Government guarantees. Industry has been talking to the Treasury about Government guarantees to the extent of about £50-£100m, callable in 1984. Total cash requirements, which would be covered by such support, will increase from the present £100m to about £180m between now and the end of ICL's financial year at the end of September this year.
5. If the company went down the tubes, there would be serious problems for the customer base, including all Government installations using ICL equipment; the UK clearers would, as already mentioned, only lose about £10m, but there would be about £100m overseas; ECGD would lose about £120m.
6. It is likely that ICL will be approaching the Government for bridging guarantees on these lines within the next day or two.



JOHN HOSKYNS





10 DOWNING STREET

From the Principal Private Secretary

11 February 1981

econ pol  
dec 79 vrs  
cc: Cabinet  
co  
Gron BL

Dear Jim,

Future of ICL

The Prime Minister has seen and taken note of the Lord President's minute of 9 February 1981 about the likely consequences for the Government's computing if an orderly solution is not found to ICL's problems.

I am sending copies of this letter to Private Secretaries to other members of Cabinet and to David Wright (Cabinet Office).

Yours ever,

Heri L. Williams.

Jim Buckley, Esq.,  
Lord President's Office.

205



cc. Mr Wolfson  
Mr Hoskyns.

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Prime Minister.  
This does not require  
any immediate decisions.

AKW  
10:11

PRIME MINISTER

*[Handwritten mark]*

FUTURE OF ICL

In the light of the discussion on Tuesday at E Committee, I think our colleagues should be aware of the likely consequences for the Government's computing, if an orderly solution is not found to ICL's problems.

Largely as a result of the procurement policy, the Government has some 200 ICL computers; some 70% of the Government's large computers come from the company and almost all our major computer systems, for example in DHSS, Inland Revenue, Customs and Excise and the Ministry of Defence, use them and they are an integral part of the operations they support.

ICL are responsible for the maintenance of the hardware and software of these machines; if this breaks down large areas of Government business will be in severe jeopardy. The maintenance operation is large (it costs us almost £9 million a year) and specialised; there are some small firms specialising in maintaining computers made by other firms, but they could not quickly absorb what ICL now does.

Our computer needs are constantly increasing; and we frequently need enhancements and new computers to expand existing systems. They have to be compatible with what we have; and this means they must come from ICL. For example extra computers are on order from ICL to cope with the taxation of unemployment benefits; without them we shall not be able to begin taxation and DHSS could have some problems in coping with the payment of benefits if the number of unemployed grows as is forecast. There will be other problems of the same sort.

We have some 24 large computers (excluding a further 47 for PAYE) at present on order from ICL; most of them are to replace existing machines at the end of their lives. CCTA are examining urgently with departments what the consequences of non-delivery might be. At best we should have to face the increasing unreliability of aging machines, but there may well be more serious problems.

Finally we are putting up some new systems on ICL computers; PAYE, and Camelot are examples. We shall face serious delay (including in staff savings) if we have to redesign the systems to run on other machines.

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However ICL's problems are solved, we seem likely to face some of these difficulties. I judge it likely that ICL's large 2900 range will not survive and this will face us with large conversion costs (perhaps some £150 to £200 million) and delays in new systems. But most essential is to secure the maintenance of our existing computers for at least long enough for an orderly transition - perhaps 5 to 10 years - and the delivery of at least the most urgent of those machines already on order. We shall also need to look carefully at any question of new orders to ICL (of which fortunately none seems essential before the end of March) until the situation is clearer.

I am copying this to all our Cabinet colleagues and Sir Robert Armstrong.

S

SOAMES

9 February 1981





C. Mr Walker  
Mr David

Prime Minister.

A situation report.

PRIME MINISTER

MS.

MS  
6ii

FUTURE OF ICL

In my minute of 2 February I outlined to you the recent deterioration of ICL's financial position, the discussions I had held with the management of the company and the position of Government and other users should the situation deteriorate to the point of ICL's collapse. I reported further, at the meeting of E Committee on 3 February, on the outcome of ICL's Annual General Meeting earlier that day, at which the company's borrowing limit had been raised.

2 I held a further meeting with ICL on the morning of 4 February, at which the Chairman, the Managing Director and the Finance Director explained their view of the immediate financial prospects in the light of the AGM. There were one or two encouraging signs; in particular, the AGM itself had gone well. However, the roots of the financial problem had still to be tackled and confidence in the company remained low. The share price had fallen sharply and there were signs that large customers were holding off from firm commitment to new orders on ICL. I was left in no doubt that the Board and the management team understood they had to end the current uncertainty and speculation with all speed.

3 In particular, the Finance Director emphasised that, although the newly increased borrowing powers gave plenty of theoretical head room for the rest of the company year (ending 30 September),

/there ...





there were still doubts about the readiness of their bankers to extend facilities in order to cover their foreseen borrowing needs. Like the company, the banks could see that the combination of expected losses and closure costs would so reduce the net worth again in the next year's balance sheet that the level of likely borrowing would seem totally disproportionate, in spite of the increased powers. The banks were therefore likely to be reluctant to embark on such a course without a clear view of the longer term future of ICL, but it was very hard for the company to give such a view now that the Board had concluded that a partnership or joint venture was essential. Indeed, the question for the company would become not so much whether the banks would go on lending but how far the company should be willing to go on borrowing. However, he did not expect the Board to have to face that question before the end of the month.

4 We agreed that in these circumstances the first priority must be for the company to establish firmly with their bankers what borrowing facilities would be available to cover the needs of the coming months, keeping Lord Benson fully informed of progress and reporting back to me when the position was clearer. In the light of our discussion the Chairman decided against submitting the proposal, of which we had had prior warning, for Government R and D assistance of £70 million. Both he and the Finance Director stressed, however, that they were still concerned about

/the ...





the likely absence of any element of direct inflow to the profit and loss account in what the banks could provide, without which an erosion of the company's net worth could not be prevented.

5 In parallel, ICL would be opening confidential negotiations with prospective partners. They are to have further discussions with Univac in London on Monday. The Chairman wanted us to be in no doubt, however, that the ICL Board would see a direct link between the length of time available for negotiations, which would depend on the availability of financial cover, and the extent to which UK interests - including those of Government users - could be secured in the negotiations. If it proved impossible to obtain a satisfactory financial package soon enough to keep the business running in accordance with accounting prudence, ICL would have to seek an immediate takeover in which those interests could not be guaranteed. I acknowledged the force of the point but said that in any case I was sure ICL would have to move fast to avoid rumours and leaks. They should aim to secure Heads of Agreement with a suitable partner within months. I agreed that advice would be provided on the way we would wish to see user and other national interests treated within a partnership or joint venture.

6 Later the same day Sir Peter Carey discussed the financial position of ICL with Lord Benson, who confirmed that there was an urgent need to act in order to prevent loss of confidence and a further rapid deterioration. As a result, the Bank of England





have now agreed to take the lead in calling together ICL's bankers for an urgent assessment of the company's immediate needs and the ways they might be met, in the context of the clear intention to seek a partnership to secure the longer term future. ICL have been briefed on what is happening and will of course be directly involved. Officials here will keep in close touch with the progress of the assessment and will work together with the Central Computer and Telecommunications Agency in providing technical support and ensuring that the interests of the Government users are given full weight. I will report further to E Committee when the picture is clearer.

7 I am sending copies of this minute to other members of E Committee, to Patrick Jenkin, Mark Carlisle, Sir Robert Armstrong and to Mr Ibbs.

KB

6 February 1981

KENNETH BAKER



070  
CONFIDENTIAL



600 P01  
/ KH  
Mr Whitman - 600

to su

CABINET OFFICE

70 Whitehall, London SW1A 2AS Telephone 01-233 8319

From the Secretary of the Cabinet: Sir Robert Armstrong KCB, CVO

R

Ref: A04202

6th February 1981

Dear Tim, R H

Ministerial Committee on Economic Strategy:  
International Computers Limited

returned to  
Cabinet Office  
22/9/81

I enclose a Most Confidential Record of the discussion on ICL at Tuesday's meeting of the Economic Strategy Committee. There are only three copies of this record: in addition to the one enclosed with this letter one is being held here in Sir Robert Armstrong's office, and I am sending the third copy (together with a copy of this letter) to Ian Ellison (Industry). No further copies are to be taken of this MCR.

Yours ever,

David

D.J. Wright

T.P. Lankester, Esq



CONFIDENTIAL

PRIME MINISTER

Future of International Computers Limited

BACKGROUND

You asked for a preliminary discussion at the meeting of E this afternoon of the minute of 2nd February from the Minister of State, Department of Industry to you about the future of ICL.

2. The position seems to be that, unless ICL can muster sufficient short-term financial support by mid-February, they could be forced to make a quick sale to an overseas company or to go into receivership. If, however, they could secure a credible package to tide them over, they would then over the coming months try to negotiate a joint venture; I understand that Sperry Univac and either Hitachi or Fujitsu of Japan are the front runners. The ICL Board has already formally accepted that the company cannot continue in the computer business in its present independent form.

3. Speculation on the future of the company will increase after the Annual General Meeting this afternoon at which the Chairman will announce a substantial trading loss for the first half of the year. The share price has now fallen to 45p from a peak of 196p in 1980. The deterioration in prospects emerged around the middle of 1980, when the collapse of ICL's export market was followed by a sharp fall in business in the United Kingdom (and the latter represents only 50 per cent of total business but 90 per cent of profits). The Financial Times - page 6 today - are already commenting on the problems and on the possibility of Government aid.

4. In the meantime ICL are talking with the Bank of England and with their own bankers - Midland, Barclays, National Westminster and Citibank. The shareholdings are now widely dispersed, and I understand that the institutions collectively hold not more than around 10 per cent. It does not, therefore, seem likely that they will be a source of support.

5. It is argued that the banks' assistance will be limited by the fact that ICL are already near to their maximum borrowing levels and that the company might need £70 million over two years from the Government, of which

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£50 million would have to be put in before September 1981. It would be given under the powers of the 1968 Science and Technology Act and in support of research and development under the Department of Industry's Process and Product Development Scheme (PPDS). ICL already get around £3 million a year under this scheme and since it would not be a new form of aid it should not be necessary to get clearance from the European Commission. If it were to be given in this form, I think that you could justify it in relation to what you said to Brian Walden in your Weekend World interview on Sunday (see the attached extract from the transcript). The Government would not be taking a stake in the ownership of the company; and the selective assistance would be under existing legislation, although not under the powers relevant to development areas.

6. Because of the size of the proposed sum it is almost certain that a claim on the Contingency Reserve would be necessary.

7. The Government has not had any stake in the ownership of the company since the NEB sold its holding in December 1979 (there could be some - unjustified - criticism that the NEB were sharp in selling at 120p a share before the price collapsed to the present 45p). The case for intervention by the Government would be:-

- (i) Thanks to the computer preference policy, a number of Departments and other public sector users are now heavily dependent on ICL, and would be faced with substantial conversion costs if there were to be precipitate sale to a new supplier - see paragraph 4 of Mr. Baker's note.
- (ii) Overseas users, who were encouraged by the Government to buy from ICL, would also be hit at a cost to the general reputation of United Kingdom exporters - Mr. Baker's paragraph 5.
- (iii) Some support is necessary to buy time and to secure the orderly sale of what ought to be a good business - it has about £2 billion of its equipment around the world and its sales outlets ought to be highly attractive to prospective purchasers.

8. It is proposed that, if further assistance is to be given by the banks and/or by the Government, urgent changes in ICL's top management are necessary. The present Chairman is Philip Chappell, formerly of Morgan Grenfell, and appointed in December 1979 despite the doubts of the Secretary of State for Industry and the outgoing Chairman. DoI officials regard him as a disaster.



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HANDLING

9. You will wish to invite Mr. Baker to speak to his note and to report on the reaction to today's Annual General Meeting. The Secretary of State for Industry will wish to comment, although he will not be fully up-to-date with developments during his visit to Germany. The Chancellor of the Exchequer will wish to give his provisional views on the case for financial support and the further discussions which must follow. The Lord President of the Council can explain the acute difficulties which will be faced by Government Departments using and currently ordering ICL equipment if there were to be a precipitate collapse. The Secretary of State for Employment might want to comment on employment implications - ICL employ about 23,000 people in the United Kingdom.

10. More work and negotiations are necessary before the case for action by the Government can be fully evaluated, and I suggest that the Committee should treat this as a "second reading" discussion and should not come to any firm decision today, either for or against support.

11. If the provisional judgment is that the consequences of sudden collapse would be so damaging to both public sector and other interests that some form of support is essential, you will need to consider what points should be taken in the further discussions. In particular:-

- (i) You will wish to be satisfied that it is indeed the case that the banks cannot deal with the problem without Government assistance.
- (ii) If there is to be Government assistance, consideration should be given to looking for some return in due course by way of, for example, a levy on future profits. But this arrangement was made for £40 million of R & D assistance given in 1972-73 and, even before the present crisis, the PAC had been informed that ICL's profits were too low for the expected levies to be paid.
- (iii) Should it be for the banks rather than the Government to take the lead in bringing about the necessary top management changes? The more the Government is involved, the more it will be vulnerable to criticism of getting back into the driving seat of this company.



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12.. You will also need to consider the next immediate steps. The negotiations will have to be strictly confidential and conducted by the Department of Industry, the Treasury and probably the Civil Service Department, in consultation with the Bank of England. The Secretary of State for Industry will then have to report back as soon as necessary, and the Committee might need to consider the matter urgently very soon.

13. In the meantime you will wish to impress on the Committee the importance of not saying anything which could further undermine confidence in the company. If it becomes known that the Committee had discussed ICL today, it should be played down as a short general discussion in the light of the situation revealed by the Annual General Meeting.

CONCLUSIONS

14. You will probably wish to sum up by inviting the Secretary of State for Industry:-

- (i) to arrange for officials of his Department, the Treasury and the Civil Service Department to consult urgently with the Bank of England and the company on the next steps and, in doing so, to take account of the general points made in the Committee's discussion;
- (ii) to report as soon as necessary on the outcome;
- (iii) in the longer term, and in consultation with the Lord President of the Council, to consider the implications of the takeover of ICL by an overseas company for the Government's computer procurement policy.



Robert Armstrong

3rd February 1981



Well, I'm trying always, as you know, to be candid with you.

but honestly these decisions are very, very difficult.

BRIAN WALDEN:

I know that. But I smell something of real importance there.

You said you never want to take on anything like Leyland again...

MARGARET THATCHER MP:

No, I don't

BRIAN WALDEN:

So can you firmly pledge that ICL, Talbot, anybody else who comes along with the begging bowl, you're not in fact going to put a lot of money into it.

MARGARET THATCHER MP:

I'm not going to take on, as British Leyland was taken on, another.....you see we're 95% owner of British Leyland.

I just can't take that on....

BRIAN WALDEN:

And you're not going to do that again?

MARGARET THATCHER MP:

No, no, no we've done it and I just, we can help sometimes, you can do selective help, but never, never, never take on the ownership.

BRIAN WALDEN:

Ah, I'm a bit worried about selective help. How much does selective help cost as opposed to what Leyland has cost?

MARGARET THATCHER MP:

Well I think you're reading more into what I'm saying than I intend. You've got companies in the development areas.



expand in those areas there shall be help for them. You've already got a budget for that, that's what I mean by selective help. Let me give you an example .....

BRIAN WALDEN:

What about Talbot or ICL then? Supposing they come along, are you going to give them selective help?

MARGARET THATCHER MP:

If they're slap right in the Midlands or if they're slap right in a non-development area, they do not qualify under existing legislation.

BRIAN WALDEN:

And they won't get it?

MARGARET THATCHER MP:

And they won't get it. If in fact they're in the development areas they already qualify for help .....

BRIAN WALDEN:

Of course.

MARGARET THATCHER MP:

under existing legislation. Just let me give you an example. I also was very worried about Bowaters when they put newsprint right out. Now there were things that we could have done and that we offered to do, well within government and nationalised industries' power to help, well within the legislation. One of the things was that if they expanded there and really modernised they would have got help under existing Industry Acts within existing budgets. Now this is why I'm making it clear, some people say well that was government help. It was help in fact, under existing budgets,



4 March 1981

Policy Unit

SECRET

*lai*

PRIME MINISTER

ICL

*mk*

Ken Baker rang me today to give me advanced warning of ICL developments. The position is as follows:

1. There are three potential bidders, in order of likelihood and suitability: Sperry Univac, [Control Data Corporation,] Fujitsu.
2. ICL Directors are a bit jittery, have been taking advice about their personal positions. There is a lack of confidence in the City for obvious reasons.
3. Total overdrafts are about £110m, but only about £10m of this is with the home clearers. The main exposure of £100m is overseas and ranks lower down in the debt queue.
4. The clearers would help with financial support provided there are Government guarantees. Industry has been talking to the Treasury about Government guarantees to the extent of about £50-£100m, callable in 1984. Total cash requirements, which would be covered by such support, will increase from the present £100m to about £180m between now and the end of ICL's financial year at the end of September this year.
5. If the company went down the tubes, there would be serious problems for the customer base, including all Government installations using ICL equipment; the UK clearers would, as already mentioned, only lose about £10m, but there would be about £100m overseas; ECGD would lose about £120m.
6. It is likely that ICL will be approaching the Government for bridging guarantees on these lines within the next day or two.



JOHN HOSKYNS



PRIME MINISTERINTERNATIONAL COMPUTERS LIMITED

1. This is to be raised orally at E. Before we can think about whether to help ICL, we need more background information:
- (1) How much of the problem is due to the exchange rate? What would their cash position have been if the pound had followed a different path over the past year? (I understand that the exchange rate started to bite in the first half of 1980 and that approximately half their sales volume is exports.)
  - (2) How much of the problem is due to sudden collapse of demand? (I understand the UK market suddenly went flat in the middle of 1980, for the first time since 1972. I know from experience that collapse of demand in the computer industry can be very sudden, when it does happen.)
  - (3) Ken Baker says that the ICL Board accepts that the company does not have an independent future. To what extent is this the result of long-term strategic appraisal (market development, international competition, technological change etc) and how much of it is the result of the cash crisis? (Many have said that ICL's product and market strategy is wrong, for some years; but I understand that only the cash crisis focussed their minds.)
  - (4) Is there any analogous experience, here or perhaps in the States, about the likely problems for customers, whether rental or purchase, where a computer supply collapses? (I think in the past, for example in the case of RCA, the buyer has picked up the customer rental base as part of the deal. He can afford to since, with no further technical development of that hardware, the rental base becomes a "cash cow"; and he can't afford not to, because he wants those customers to move to his own equipment in due course.) The scenario painted by CSD (paragraph 4 of Ken Baker's minute) seems unlikely except in the case of receivership. But in that



case continued servicing of existing customers might still be possible.

2. ICL of course raises a more general question about intervention, on which we do not have a properly thought out position. Ownership of the shares - whether prudential, a pension fund, or HMG - is irrelevant. If the Government is interventionist, then it should help ICL. If it is not interventionist, it should not be helping BL or BSC.



COMMERCIAL IN CONFIDENCE



**DEPARTMENT OF HEALTH & SOCIAL SECURITY**

Alexander Fleming House, Elephant & Castle, London SE1 6BY

Telephone 01-407 5522

*From the Secretary of State for Social Services*

3 February 1981

Tim Lankester Esq  
Private Secretary  
10 Downing Street  
LONDON  
SW1

*Dear Tim,*

I see from Jonathan Hudson's letter of 2 February that the situation of ICL will be discussed at "E" Committee today. As my Secretary of State will not be present he felt it might be helpful to colleagues if we summarised our interest. As the major government user of ICL equipment (our departmental investment currently exceeds £40 million) and because of our responsibilities for the NHS (where there is an investment in ICL equipment of some £17 million) we have two objectives:

- (i) to ensure the provision of equipment needed urgently for operational reasons, eg to enable the rising unemployment register to be handled and to facilitate the taxation of benefits for the unemployed from April 1982; to implement our CAMELOT project.
- (ii) to maintain the operation of existing ICL installations engaged on social security and NHS work and engineer an orderly transition, over a long time span, to a future system.

For these reasons we see maintaining confidence in ICL as an important step in the process of negotiating a deal which would offer realistic prospects of future viability and at the same time protect our essential interests.

I am copying this letter to the Private Secretaries of the Members of "E", the Secretary of State for Defence, Sir Robert Armstrong and to Jonathan Hudson.

*Your ever*  
*D Brereton*

D Brereton  
Private Secretary



cc. Mr Wolfson  
 Mr Walker  
 Mr Haslegrave  
 Mr Ingham.



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PRIME MINISTER

FUTURE OF INTERNATIONAL COMPUTERS LIMITED

1 In Keith Joseph's absence abroad I am writing to let you know of a sharp deterioration in the situation of the Company, the full extent of which has been revealed to this Department by ICL during the past ten days. The matter is likely to become the subject of increased Press speculation after the Annual General Meeting of shareholders tomorrow at which the Chairman will announce a substantial trading loss for the first half of this Company's year and immediate profit shortfall against corporate plans. The forecasts are, in fact, for a pre-tax loss of £25m - £35m for the year to 30 September 1981 and for a level of borrowing which is in danger of exceeding firmly-available facilities in peak months before end September.

2 This situation is attributable primarily to the worldwide recession, the strength of sterling and increasing competition for computer products. But management acknowledges that it also stems from their own failings, in particular to control the rise in costs during the year. The Company is taking a range of measures to help improve the situation - e.g further factory closures; reduction of up to 2500 manufacturing and development staff; no wage increase this year. These cannot bring relief until after the end of the current Company year and some of these measures will in fact contribute to the loss in this year.

13 ...

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3 The ICL Board has now formally accepted that the Company cannot continue in the computer business in its present independent form. I have told the Chairman and Managing Director that it must enter into some form of joint venture or partnership which will inevitably involve a major change in the shareholder structure and control. The Company recognises this. No British-owned company has so far displayed any interest in such an arrangement but the Company has had preliminary discussions with the US company, Sperry Univac, and with the Japanese company, Hitachi, though I do not rule out other possible Japanese partners. It will follow-up the necessarily confidential discussions urgently, but estimates that it could take up to twelve months to negotiate a deal which would offer realistic prospects of future viability and at the same time protect the essential interests of the existing customer base.

4 The Civil Service Department estimates that, if the Company has to sell-out precipitately to an overseas' company without adequate safeguards, or goes into receivership, the costs of converting software and equipment to a new supplier could be between £150m and £200m for central Government alone. This estimate excludes the similar costs which would have to be borne by other public sector users (e.g universities; NHS; local government; nationalised industries).

/5 ...





5 The effects on users outside the UK public sector would be most damaging in sensitive areas like the European Community, the European Space Agency and the oil states, where much diplomatic effort has secured strategically important sales for ICL.

6 There are solid arguments, therefore, for assisting the Company to survive its present short-term difficulties so that it can obtain the right sort of partner and secure the longer term future for this important part of our information technology industry. I have told ICL that it must seek support from the market. It is therefore in close touch with the Bank of England, and with its own bankers, to see whether the banking community is able to put together a credible short-term support package. Present indications are that, even if the banks can put together such a package, (and they, in common with the customer base and other parts of the information technology industry do not want to see ICL collapse) there will probably be a need for supplementary support of some kind from Government. Until we have had further consultation with the Bank of England this week the form and extent of such assistance cannot be determined. The company believes that, in order to maintain its legal borrowing levels, some part of the support will have to flow into its profit and loss account and that the banks' contribution will not include this essential element. It puts this requirement at £70m over two years.

/7 ...





7 In the coming day or two ICL intend to propose specifically that we should meet this need by contributing £70M (£50M in the current company year) to the maintenance of the company's R and D, product launch and market development programme in order to keep up the essential impetus of new product introduction. This would ensure that it was able to conduct confidential partnership negotiations from a stronger position, which would offer the prospect of securing customer and employee interests. It would also help to maintain the confidence of banks and customers through this vital transitional stage.

8 My officials are in close touch with the Company on its handling of (and statements to be made concerning) the AGM and on the way in which it is determining and exploring the various options open to it. They are also in close touch with the Bank of England, with the Treasury and with the CSD concerning the interests of the Government users. I am convinced that it is absolutely fundamental to any credible and viable solution that there must be changes in the senior management of the present Company. This may take some time to effect but my own view is that, as a condition precedent to any financial support package by the banks, and possibly Government, someone of stature must be appointed at once to the Board specifically charged to drive forward the negotiations with a prospective partner in a manner acceptable to us. A vital corollary will be action to maintain the confidence of customers in ICL and its products while negotiations are concluded. We obviously have a role here.

/9 ...





9 No doubt you and other colleagues will wish to discuss this matter after the Secretary of State's return when we know the outcome of the Company's AGM and what the banks are likely to be able to offer.

10 At this stage, I am copying this minute only to the Chancellor, the Foreign Secretary, the Lord President and also to Sir Robert Armstrong and to Mr Ibbs.

*K.B.*

K B

2 February 1981

Department of Industry  
Ashdown House  
123 Victoria Street



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DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB  
TELEPHONE DIRECT LINE 01-212-6401  
SWITCHBOARD 01-212 7676

From the  
Minister of State's Office

Kenneth Baker MP

Tim Lankester Esq  
Private Secretary to  
The Prime Minister  
10 Downing Street  
London SW1

2 February 1981

*Dear Tim,*

*TL*

INTERNATIONAL COMPUTERS LTD

I understand that the situation of ICL is to be discussed at 'E' Committee tomorrow. I therefore attach for those who have not seen it, a copy of Mr Baker's minute of today's date to the Prime Minister.

I am copying this to the private secretaries to the Members of 'E', the Secretaries of State for Defence and Social Services, Mr Ibbs and Sir Robert Armstrong.

*Yours sincerely,  
Jonathan Hudson*

JONATHAN HUDSON  
PRIVATE SECRETARY



Mr R A Lingard  
Hd IT 3

#### POSSIBLE ASSISTANCE TO ICL

1 At our meeting on 26 January with Mr Stuart of ICL you asked me to endeavour to substantiate the performance forecasts for ICL contained in the Company's note dated 13.1.81 with particular reference to the cash flow forecast and bank borrowing requirements. I had discussions with Mr Stuart and Mr Ellis (Deputy Managing Directors) Mr Bishop (Company Treasurer) and members of his staff. My findings are as follows.

2 My enquiries centred on the UK cash flow forecast attached as Annex 1 hereto which was supported by a number of schedules covering the assumptions made and bases used in forecasting and detailed calculations. I am satisfied that the information presented to me was the same as that being presented to management and that the Company's representatives were being entirely open with no hint of duplicity. I concluded that the forecasts had been carefully prepared and, with the exception of sales revenue, there was little potential for material variances from the forecast figures.

3 Total sales are estimated at £740m to include equipment sales of £420m. It is not considered that sales revenue from maintenance and software are likely to be the subject of material variation but equipment sales might reach a maximum attainable figure of £460m and a corresponding minimum level of £380m. Additional sales would be delivered from stock and would not involve any additional cash outlay at the manufacturing stage although debtors could increase by some £10m. £40m additional turnover is therefore likely to lead to an additional cash generation of £30m. Conversely a sales short fall of £40m is unlikely to save manufacturing or other cash outlays although debtors could be reduced by, say, £5m giving an additional cash requirement during the year of £35m. The recent adverse publicity is likely to have reduced confidence of potential customers for ICL and the 1980/81 out-turn for equipment sales is more likely to produce an adverse variance against forecast than a favourable variance.

4 The year end UK overdraft of £95.7m shown in Annex 1 assumes the maximum utilisation of overseas borrowing facilities so as to give a year-end overdraft world-wide of £138.2m. The same forecasting techniques however indicate a peak world-wide borrowing in mid August of £192m. The maximum world-wide overdraft requirement during 1980/81, assuming a £40m sales short-fall, is therefore of the order of £227m.

5 Inventories, particularly stocks of finished products, are excessive. A possibility of realising cash by stimulating sales with price reductions has been considered and implemented to some extent but the scope for pursuing this policy is limited by a need to preserve the goodwill of existing customers. Inventory reduction through reduced manufacturing activity is also being implemented and should improve profitability in 1981/82 but redundancy costs prevent any cash flow benefits being obtained in 1980/81.

6 I have not examined the 1981/82 cash flow forecast but it is thought that the manufacturing programme would by then have been brought into line with sales demand so as to allow an inventory reduction sufficient to reduce the cash out flow to much more manageable proportions than during 1980/81.

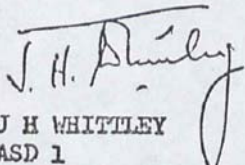


7 At Annex 2 are shown the bank facilities currently available to ICL. Additionally the Company has facilities of £150m for the "off balance sheet" financing of leases and £178m to finance export sales under ECGD guarantees but these sources of finance have been taken into account in arriving at the borrowing requirement discussed above. The available facilities barely exceed the possible borrowing requirement noted above and not only are many of the facilities renewable as soon as March 1981 but also some are repayable on demand. Any loss of confidence by bankers in ICL could lead to a withdrawal of facilities leaving the Company with insufficient cover.

8 I understand, though have not been able to substantiate, that the borrowing powers of ICL directors are limited to two times the share capital and reserves as shown by the latest published consolidated balance sheet. I also understand that a special resolution is to be proposed on 3 February next to increase borrowing powers from two times to three times net worth. At 30/9/80 the Group's net worth was £141m thus the directors borrowing powers are currently £282m and are expected to become £423m. The present limit is barely adequate to cover projected borrowings including export finance and unredeemed debentures of £15m.

9 The profit and loss account projection for 1980/81 corresponding to the cash flow forecast for that year is for a loss of £35m and for 1981/82 a further loss of £28m. Even if the borrowing powers are increased to three times net worth and if the results are as forecast the directors borrowing powers will be reduced to £318m when the 1980/81 accounts are published and to £234m one year later. It is to prevent a reduction of borrowing powers consequent upon a reduction of reserves that ICL are looking for a contribution to revenue in 1980/81.

10 If you require further comment or information please do not hesitate to let me know.

  
J H WHITTLE  
ASD 1  
Room 725 Millbank Tower  
211 3239  
30 January 1981

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U.K. CASH POSITION (£ MILLIONS)

ANNEX 1 to ASD minute  
dated 30 January 1981

	Qtr 1	Qtr 2	Qtr 3	Qtr 4	Full Yr
<u>IN FLOW</u>	Actuals	F'cast	F'cast	F'cast	Total
U.K. Divisions	75.3	98.6	88.9	104.4	367.2
Education INST	1.4	1.2	1.2	1.2	5.0
Dataskil	3.3	3.5	3.8	4.0	14.6
Overseas: ID	18.9	17.9	7.1	21.3	65.2
ED	21.2	13.5	3.3	23.5	61.5
G.P.C.D Ireland	1.9	1.3	1.0	2.4	6.6
Export Finance M/T	4.1	5.3	5.5	6.6	21.5
" " S/T	9.7	19.7	9.7	19.7	58.8
Computer Leasings Div & Int	0.5	0.6	0.7	0.7	2.5
" " Trading	4.1	2.0	0.3	-	6.4
Own Use Leasings	2.7	-	-	-	2.7
Baric,	0.9	0.3	0.5	0.7	2.4
UKAEA etc	1.6	-	-	-	1.6
Miscellaneous	1.9	-	-	-	1.9
DoI	-	0.5	1.5	4.8	6.8
	147.5	164.4	123.5	189.3	624.7
<u>OUTFLOW</u>					
Regulars Inc Payroll	74.4	85.2	81.2	77.7	318.5
Suppliers	49.3	38.1	45.4	45.4	178.2
Interest	6.0	2.7	6.0	6.2	20.9
Computer Leasings	3.6	4.3	-	6.2	14.1
IC(Rentals)Own Use	1.8	1.9	1.9	1.9	7.5
MICL etc	1.8	1.2	1.2	1.2	5.4
Export Finance M/T	6.4	14.0	6.1	7.5	34.0
" " S/T	4.1	19.2	9.7	19.7	52.7
H.P. Capital + Interest	3.2	3.3	1.7	1.7	9.9
ICL Inc U.K	7.2	7.6	5.7	5.8	26.3
Miscellaneous	2.5	1.5	1.5	1.5	7.0
CPI/Singer/Debentures	3.2	-	-	-	3.2
Schedule F /Div	0.6	2.7	1.2	-	4.5
VAT	4.9	7.5	3.5	4.5	20.4
Redundancies	0.2	3.0	6.6	6.6	16.4
	(169.2)	(192.2)	(171.7)	(185.9)	(719.0)
NET IN/(OUT) FLOW	(21.7)	(27.8)	(48.2)	3.4	(94.3)
BALANCE B/F	(7.4)	(29.1)	(56.9)	(105.1)	(7.4)
U.K. STERLING BALANCE	(29.1)	(56.9)	(105.1)	(101.7)	(101.7)
IMPRESTS	2.6	2.0	2.0	2.0	2.0
CHEQUES HELD	4.4	4.0	4.0	4.0	4.0
	(22.1)	(50.9)	(99.1)	(95.7)	(95.7)



BANK AND LEASING LINES AVAILABLE

To ICL AS AT 31ST DECEMBER, 1980

I - BANK LINES

<u>COMMITTED LINES</u>	<u>£M</u>
BARCLAYS	32.0
MIDLAND	42.0
CITIBANK	24.5
NATWEST	<u>10.0</u>
SUB TOTAL	108.5
<u>OTHER U.K. LINES</u>	63.2
<u>OVERSEAS LINES</u>	63.3
<u>TOTAL LINES WORLDWIDE</u>	<u>235.0</u>

NOTE: COMMITMENT:

- NATWEST TERMINATES 31ST MARCH 1981
- CITIBANK TERMINABLE AT ANY TIME IN AN AMOUNT OF £8.5M: BALANCE IS COMMITTED TO MARCH 1983.
- MIDLAND TERMINABLE AT ANY TIME IN AN AMOUNT OF £10M: A FURTHER £10M TERMINABLE 10TH MARCH 1981: BALANCE IS COMMITTED TO FEBRUARY 1982.
- BARCLAYS IS COMMITTED TO 3RD FEBRUARY 1982
- SOME £42M IS PRESENTLY DRAWN FROM THE LONDON MONEY MARKET, SOME £15M OF THIS RUNS OUT IN MAY 1981: THE BALANCE EXPIRES IN NOVEMBER 1981.
- ALL OTHER LINES WORLDWIDE ARE ESSENTIALLY PAYABLE ON DEMAND.



3 January 1981

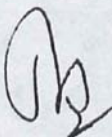
Policy Unit

PRIME MINISTER

INTERNATIONAL COMPUTERS LIMITED

Original  
returned to  
J. Hoskyns.

1. The first thing is to get some more background information:
  - (1) How many people does ICL employ and where? How big a cutback has already taken place? In which areas of the business?
  - (2) How much of the problem is due to the exchange rate? What would their cash position be, had the pound followed a different trajectory?
  - (3) How much of the problem is due to sudden collapse of UK demand? From my own experience, computer industry demand can collapse very suddenly as it did in 1972.
  - (4) Ken Baker says that the ICL Board accepts that the Government does not have an independent future. Is this the conclusion of ICL's own strategic planning? Or a panic reaction to the cash crisis?
  - (5) The CSD scenario (paragraph 4 of Ken Baker's minute) may be alarmist unless there is precipitate receivership. If someone buys ICL, the customer base is the crucial part of what he buys. He wants its cash flow in the short term, its goodwill for his own products in the long. Much depends on whether the buyer's hardware/software is compatible with ICL's. Is this the case with, for example, Sperry Univac and Hitachi?
  
2. ICL raises a more general question about Government involvement. All Governments are forced to intervene in crisis situations from time to time. We could have taken the position that we would never do so in any circumstances, though I don't think that that would have been right. In any case, that position is no longer tenable. What we do need is a position of "coherent pragmatism". Given limited funds, to which industries do we provide terminal care because they don't have a future? Which growth industries should we favour (as on PAYE for ICL) and help in real emergency? Regardless of who owns the shares, it seems to me very difficult to let ICL go, for want of £70m, after the help we have given to BL and BSC.



JOHN HOSKYNs



RESTRICTED

*Com M*

Caxton House Tothill Street London SW1H 9NA

Telephone Direct Line 01-213 6400

Switchboard 01-213 3000

GTN 213

The Rt Hon Lord Soames GCMG GCVO CBE  
Lord President of the Council  
Civil Service Department  
Whitehall  
London SW1

*Ray*

23 December 1980

*Dear Christopher*

I have seen a copy of your letter of 12 December to Geoffrey Howe about the PAYE and Customs and Excise contracts.

I agree that both these contracts should be signed with ICL before the end of the year. In my view the safeguards which have been achieved in the case of the PAYE contract (and which the CCTA hope to secure for the Customs and Excise contract) are more than we could reasonably have expected.

I am copying this letter to the recipients of yours.

*Yours  
T*



01-405 7641 Ext.

*Communications on this subject should  
be addressed to*  
THE LEGAL SECRETARY  
ATTORNEY GENERAL'S CHAMBERS

ATTORNEY GENERAL'S CHAMBERS,  
LAW OFFICERS' DEPARTMENT,  
ROYAL COURTS OF JUSTICE,  
LONDON, W.C.2.

22nd December 1980

A J Wiggins Esq  
Private Secretary to the Chancellor  
of the Exchequer  
H M Treasury  
Treasury Chambers  
Parliament Street  
LONDON SW1P 3AG

12  
2714

*Dear Wiggins*

PAYE COMPUTER CONTRACT

With regard to the first sentence of paragraph two of the Chancellor of the Exchequer's letter of 18 December, I should like to record that the Attorney General regards himself as having advised only on the question whether the proposed contract is satisfactory with regard to the United Kingdom's obligations under the EEC Supplies Directives. Whether the terms are otherwise acceptable is a question of policy for Ministers.

Copies of this letter go to private secretaries to the Prime Minister, Members of E Committee, the Secretary of State for Defence, Robin Ibbs (CPRS) and Sir Robert Armstrong.

Yours sincerely,

*Alan D. Preston*

A D PRESTON





*Ecan Pool*

Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

The Rt Hon Sir Geoffrey Howe, QC, MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
LONDON SW1P 3AG

19 December 1980

*Dear Geoffrey,*

*M  
20/12*

PAYE CONTRACTS

I am rather surprised by the tone of your letter of 18 December. If colleagues decide that we must negotiate and sign a major contract such as this within a matter of weeks is it surprising that there are still question marks? I don't get the impression your letter invited me to comment on the detailed points which you raised but I want to make it clear that I believe that my people have done a superhuman job in covering as much ground as they have in the time available. I could not have asked for more.

I am copying this to recipients of your letter.

*Yours ever*

*Christoph*

SOAMES





01-405 7641 Extn

ROYAL COURTS OF JUSTICE  
LONDON, WC2A 2LL

*Eca Pd*

18 December 1980

The Rt Hon Lord Soames GCMG  
Lord President of the Council  
Civil Service Department  
Whitehall  
LONDON SW1

*T2*  
*28/12/80*

*Dear Christopher,*

After receiving your letter of 12 December seeking agreement to the signing of the PAYE and C & E contracts, I advised that certain provisions of the Break Clause in the PAYE contract (other than those referred to in your letter) were unsatisfactory from the EEC point of view and advised how in my view they might suitably be amended. I am now informed that agreement has been reached with ICL on this and a number of other minor amendments and I can now say that I see no legal objection to this contract being signed.

I have not seen the C & E contracts but I am told that the CCTA have been advised of the dangers from the EEC point of view of building too much flexibility into these contracts.

I am sending copies of this letter to the recipients of yours.

*Yours* *W.C.*

*Michael*

\_\_\_\_\_



CONFIDENTIAL

*of Bygones*



Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000 18 December 1980

The Rt Hon The Lord Soames GCMG GCVO CBE  
Lord President Of the Council  
Civil Service Department  
Whitehall  
LONDON SW1

*MBM*  
*R. 12/12*

*I. Whitson*

Your letter of 12 December asked me and colleagues to let you know early this week whether we agree that the PAYE and Customs and Excise contracts should be signed with ICL before the end of the year on the basis you outlined.

If the Attorney General is content with the contractual safeguards written into the Agreement than I am prepared to accept your advice that the contract with ICL should be concluded before the end of this year, but I still have some serious concerns. For example, I cannot say that I am very happy with a draft Agreement which specifies hardware and software costs but which refers to other costs or services which may or may not be incurred without putting figures to them. I understand from my people that chargeable support, testing proposals and facilities and the like could add another million pounds to the cost over the implementation period. Nevertheless, if it is your judgement that these charges are reasonable and acceptable, then I concur.

More serious are the continuing technical reservations. No one has had a chance to make any detailed evaluation of ICL's formal technical response to the Revenue's Operational Requirement and yet even without that you tell us that the CCTA view is that the delay to the project likely because of ICL's technical shortcomings will now be more than 6 months and could be up to a year. As you know, the cost in terms of staff savings foregone is £50 million a year. My fear is still that the technical weakness of the ICL offering may damn the project to technical instability during implementation. The very serious reservations you express in your letter give me little confidence in taking ICL's promises on trust.

/Moreover, assuming



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Moreover, assuming that we shall want to continue with the computerisation of PAYE until the whole process is complete, the contract locks us in with ICL over what may prove to be the best part of 10 years, even if their performance is in the event less than satisfactory but falls short of completely falling down on the job. Equally, we shall be prevented from taking advantage of significant technical advances made by ICL's competitors so that we may have to go on putting in obsolete machinery to work an obsolete system. I do not view that prospect with any favour.

However, we have been over all this ground before. The risks to the project from committing to ICL remain substantial, even though my people tell me that they expect that in time the ICL solution should be made to work satisfactorily. I see no alternative to going ahead but I warn colleagues that the timetable for the completion of the computerisation project must remain uncertain for some time to come. The draft Agreement with ICL provides no indemnity against that. Not the least because of this and the very heavy costs that delay imposes, if ICL fail in the demonstration that must be the end of the matter.

So far as Customs and Excise is concerned, as I said in my letter of 12 December to you, which seems to have crossed with yours, I am content to go to Single Tender.

I am copying this to the Prime Minister, members of E Committee, the Secretary of State for Defence, the Attorney General, Robin Ibbs (CPRS), and Sir Robert Armstrong.

A handwritten signature in black ink, appearing to read 'Geoffrey Howe', with a horizontal line above and below it.

GEOFFREY HOWE



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cc ~~Wolsten~~  
Hoskyns  
Econ Rd



Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

The Rt Hon Sir Geoffrey Howe, QC, MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
LONDON SW1P 3AG

12 December 1980

Dear Geoffrey,

ASAM  
2/17/12

I was invited (E(80)31st, item 1) to negotiate toughly with ICL to secure the prompt and efficient performance, and the best possible value for the taxpayers' money in meeting the PAYE requirement. I was also asked to ensure that the contract was signed before the end of the year.

The CCTA have been negotiating intensively with the company who have co-operated well. The contract itself is complex and detailed, and this letter can only draw attention to some of the main points. Most contractual details have been settled. In particular we have secured:

- a. the right to terminate the contract if ICL fail to complete a successful demonstration by 31 March 1982 (ICL propose to make their first attempt before the end of 1981);
- b. arrangements whereby ICL will have an unlimited liability to make good at their expense any deficiencies arising from poor serviceability or reliability and to bear any directly consequential capital or running costs such as buildings or staff;
- c. a formula under which if performance falls short of their claims they will provide extra equipment free of charge on the same terms as (b) above; and under which, if their equipment is more powerful, we can reduce our order without penalty.

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- d. the definition of specifications and standards which will allow other manufacturers' equipment or new technological developments to be introduced (but the practical costs and difficulties of this in some respects should not be underestimated);
- e. a call-up arrangement whereby we are committed initially to the equipment for the Development Centre and for the first regional sub-centre, and subsequently to equipment for regions only as we need it (but this will not allow us to change suppliers unless ICL default).

There is however one area where the position is not satisfactory.

Technical problems

Because of the limited time available it has not been possible for ICL to complete, or CCTA to examine, a full technical proposal and we cannot be certain that it will not differ from the drafts which CCTA have seen. This means that, although there have been considerable discussions, a lot of ICL's technical claims have to be taken on trust. In particular:

- a. There are a number of items of software, particularly those concerned with communications and recovery, which are not yet developed. CCTA have not yet been able to examine the feasibility of ICL's plans to produce these to time, and there can be no guarantee that the development will run smoothly.
- b. The technical characteristics of the way in which the local office systems will be linked up to the main frames have not been wholly defined and are unlikely to be proven until early 1982. This will delay the placing of orders for local office equipment, and may delay the Inland Revenue's programme by some months.
- c. Some errors have been found in our preliminary examination of ICL's calculations of the amount of equipment needed to do the job. The contract will safeguard us against extra costs if these or other errors reveal the need for extra equipment, but in this event there might be operating problems for Inland Revenue.

Generally the situation on the technical side is that there are large areas of ICL's proposals which CCTA have not been able to examine properly and where we cannot confirm that



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they meet the requirement. In the case of such shortcomings as have been identified CCTA has agreed with ICL, wherever possible, dates on which they will be remedied. Our position has been safeguarded contractually so far as possible. This means that, where the shortcomings can be remedied by additional equipment ICL will have to provide it free and meet our directly consequential costs, such as for buildings or extra staff, but the Inland Revenue will have to bear any extra costs of delay.

CCTA cannot be confident that they have yet identified all the technical shortcomings in ICL's proposals, but their examination so far has reinforced their view (expressed in E(80)124) that ICL's technical problems will lead to a delay of "about six months"; they now believe it is likely to be at least six months and could be up to a year. The cost of delay to the Inland Revenue is £50m a year in manpower savings they will be unable to achieve.

Price

Negotiations on price have gone very well. In total COTA have secured discounts amounting to £22m (27%). This has brought the ICL price (over a 10 year life) down to £61m, about the same level as CCTA consider we should (after discounts) be likely to pay to IBM for a similar system. It is still some £6m above the likely cost of the equipment from the supplier likely to offer the lowest price. All things considered I consider this price fair and, in the circumstances, satisfactory.

Other contracts

In my minute of 1 December 1980 to the Prime Minister I undertook to attempt to place eight further contracts before the end of the year if colleagues so wished; work to this end has been continuing pending colleagues' replies and is up to timetable.

In the case of the computers for the Devonport, Rosyth and Chatham dockyards, and the telecommunications for CRISP and Bicester we have been through all our normal contractual processes and there is no additional risk in completing contracts this year; the same is true of HMS Centurion even though work has been completed very quickly.

The situation in the Customs and Excise cases is less satisfactory. The requirement is far less complex than that for PAYE, but, because it has only just become available, less work to clarify the situation has been possible. CCTA will have no opportunity to examine ICL's technical proposals



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before letting a contract. The main danger of this is that the wrong quantities of equipment may be ordered; it is possible that other problems may emerge when ICL's proposals are examined, but there is no reason at present to expect them to be of major importance. CCTA will seek contractual arrangements to enable subsequent adjustments or remedies to be negotiated without penalty and, so far as practicable, the other contracting safeguards secured in the PAYE case. I am not yet in a position to make an assessment of any likely extra costs of hurrying the contractual process but CCTA expect to secure similar safeguards as for PAYE. There should be no significant delays in the delivery of the ICL equipment.

Conclusion

As time is short, I invite my colleagues to let me know early next week whether they agree that the PAYE and C&E contracts should be signed with ICL before the end of the year, on the basis outlined in this letter.

I am copying this to the Prime Minister, members of E Committee, the Secretary of State for Defence, the Attorney General, Robin Ibbs (CPRS), and Sir Robert Armstrong.

*Long letter is so long - But  
this time it had to be!*

*You or*

*Christoph*

SOAMES

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*Econ Pa*

PRIVY COUNCIL OFFICE  
WHITEHALL, LONDON SW1A 2AT

25 November 1980

Jim Buckley Esq  
Private Secretary to the  
Lord President of the Council  
Civil Service Department  
Whitehall  
LONDON SW1A 2AZ

*Dear Jim,*

COMPUTERISATION OF PAYE

Thank you for your letter of 21 November which the Paymaster General has seen. The Minister has asked me to say that one of the main points made in his letter of 4 November was the problem of the use of unestablished equipment. The fact that most of these early computers proved deficient in performance merely reinforces that point and indicates the likely problems to be encountered with equipment that is not going to be ready to test for another year.

However, as you say, the point is academic now that decisions have been taken. I am copying, therefore, only to the Private Secretaries to the Prime Minister, the Home Secretary, the Chancellor of the Exchequer, and Sir Robert Armstrong.

*Yours sincerely*  
*Richard Prescott*

R E S PRESCOTT  
PRIVATE SECRETARY



COMMERCIAL IN CONFIDENCE

*Elen BL*



Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

21 November 1980

Richard Prescott  
Private Secretary to the Paymaster General  
Privy Council Office  
68 Whitehall  
LONDON SW1A 2AT

*12 24/11*

*Dear Richard,*

COMPUTERISATION OF PAYE

The Paymaster General wrote to the Lord President on 4 November about the problems your office at Crawley is experiencing using established ICL equipment.

Although it will be of academic interest only, now that decisions on the computerisation of PAYE have been taken, I think we should set the record right on one point. The ICL 2900 computer systems for the Paymaster General's Office were among the first procured by Government. Most of these early computers proved deficient in performance. The problems you have experienced recently can therefore reasonably be attributed directly to the use of unestablished equipment.

I am copying this to the Private Secretaries to Members of E and to Jim Nursaw in the Attorney General's Office.

*Yours sincerely,  
Jim Buckley.*

J BUCKLEY

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*Mr Whitton  
Mr Henderson*

*Beon Rd.*

Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

*MBM*  
*[Signature]*

The Rt Hon Sir Keith Joseph, Bt, MP  
Secretary of State for Industry  
Ashdown House  
123 Victoria Street  
LONDON SW1E 6RB

18 November 1980

*Dear Keith,*

*12/11*

COMPUTERISATION OF PAYE

Thank you for your letter of 4 November. Bearing in mind our respective responsibilities in this area I am deeply disturbed that the advice which you and I are receiving is so much at odds.

For example in your letter you compare ICL's discounted price for the PAYE computer with the undiscounted price of other manufacturers and conclude that there is virtually no price difference. I am assured this is wholly misleading. Volume discounts and commutation arrangements for software charges are not unique to ICL. We shall certainly expect to benefit from them in the price we eventually pay to ICL; but if we went single tender to another company - and more so if we were to go open tender - we would expect similar and even larger discounts. Thus the price differences to which I draw attention would remain, like with like.

There is no point in trying to disguise the difference from ourselves. ICL themselves have admitted to CCTA that they are, at this stage, pricing their S3 computer about 30% above a computer of similar performance of IBM's in the United Kingdom; they are doing this for legitimate commercial reasons to safeguard their rental base of smaller machines. This fact corroborates the calculations of the difference which CCTA made and suggests that they reflect the real situation.

May I also take up another point which was recorded in the E Committee minutes? It is that the evidence of the unreliability of ICL's machines is only anecdotal. This could not be more untrue. CCTA have carefully gathered statistics over a long period which are agreed by the company, and are well known to your officials. The company are well aware of the unreliability problem of their larger machines and are mounting a major programme



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to improve it. But, even with the improvements which they have achieved and which are in prospect, the levels of reliability fall well below those of other large manufacturers. CCTA and the company have higher hopes of the S3, but these have yet to be proved in operation. We are particularly aware of this problem at present since it has just been the subject of a major reference from the Comptroller and Auditor General, and may feature in his report shortly. Your people have seen both the reference and our reply.

In view of the fact that we seem so far apart in our understandings on these points, on which (certainly in my case) we rely heavily on officials, would you not agree that it would be useful for us both to instruct our officials to get together and put to us an agreed summary. I see it as farcical and bad government that you and I should be arguing about these things.

Finally, I cannot allow to go unchallenged your comments about officials defending decisions before the PAC. Officials have had a good deal of trouble with the PAC and experience teaches them that they are in for more difficulty in squaring our decisions on the computerisation of PAYE with existing procurement policy. As I said in my letter of 28 October, this is a matter on which we will have both to take and defend our own decision. Can I take it you agree?

I am copying this letter to the Prime Minister, our colleagues on E Committee, Sir Robert Armstrong and Robin Ibbs.

*Yours ever*

*Christopher*

SOAMES





VB  
Econ Pol  
cc HMT

10 DOWNING STREET

From the Private Secretary

11 November 1980

Dear Mr Cutts

The Prime Minister has asked me to thank you and your colleagues for taking the trouble to write to her on 17 October about the Inland Revenue computer project.

The ideas you put forward are interesting, but not new. It is, of course, an old adage that 95% of the complexity of any system is needed for only 5% of the cases, although in practice the proportions tend to work out a bit differently. The computer system proposed by the Inland Revenue is intended to deal with the simpler cases within the personal tax system, those coming within PAYE, and the day to day work on those cases will be carried out by clerical staff and their supervisors through terminals in the local offices.

Most people looking at the PAYE project for the first time tend to think in terms of distributed processing using mini or micro processors, but once they grasp the full significance of both the batch processing dimension and the accommodation constraints on putting computer equipment in local offices, the picture begins to change. The plans prepared over the last two years by the Inland Revenue, guided from the outset by substantial external consultancy support, have been considered by two independent reviews. In both cases, members were drawn from the systems and software industry. They also considered the implications of distributed processing on the lines you suggest but after detailed consideration endorsed the preferred approach, that is, for an on line system based on terminals in local offices linked to computer centres where the bulk batch processes would be undertaken.

I hope that from this necessarily very brief account, you will be reassured that the current proposals for computerisation of PAYE are the result of detailed analysis and review and not just a matter of accepting "the proposals of the entrenched interests".

Yours sincerely  
Michael Pattison

D.L. Cutts, Esq.

VLS



PRIME MINISTER

You expressed interest in the heretical approach on the Inland Revenue computer issue set out in the attached letter.

Here is a note from the Treasury explaining why they think the correspondents are wrong.

If you are satisfied with this, I will reply as the Treasury have suggested.

*You better have  
already gone some  
way towards their  
argument in the  
revised specification*

*MAF*

*mt.*

10 November 1980





Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

7th November 1980

M.A. Pattison Esq.  
Private Secretary  
10 Downing Street  
LONDON  
SW1

*Dear Mike,*

You asked in your letter of 22 October for a draft Private Secretary reply to this letter from Mr D.L. Cutts and others about the computerisation of PAYE and indicated that the Prime Minister was interested in the thoughts expressed.

The two main points made are:

- a) that 95 per cent of the complexity of the tax system is needed for only 5 per cent of the cases, so that
- b) a simpler computer system, based on small machines and computer files in local offices, should be devised to deal with the simple 95 per cent of cases, leaving skilled Inspectors to handle the rest manually.

It is an attractive idea and one that is often raised, but it is misconceived. The computer system is being devised to deal with PAYE, where the bulk of simpler cases in the personal tax field are to be found, but there are 27 million of them. The day to day work on those cases will be carried out by clerical staff and their supervisors, through terminals at the local offices, and not by the highly skilled Inspectors.

Like most people who have looked only superficially at the PAYE requirement, the authors are attracted to the idea of distributed processing, with small machines in each local office and the computer files held there instead of at large centres. But the economies of scale achieved through some centralisation of the big bulk tasks (including printing) which arise in PAYE throughout the year argue convincingly for mainframe machines in computer centres rather than minis or micros in local offices. It is the centralisation

/of these





of these processes which give rise to a large proportion of the savings we expect to achieve through the computerisation of PAYE. All the reviews of this project, whether carried out by the CCTA or by experts from the computer software industry, have come to similar conclusions. The most cost effective solution of PAYE automation within a balance between cost, speed of implementation, flexibility and risk, is one tending towards a smaller number of large sites rather than in the opposite direction.

.... I attach a draft reply.

*Yours ever,*

*Richard Tolkien*

R.I. TOLKIEN  
Private Secretary



Please type

Draft Private Secretary Reply to Mr D.L.Cutts and others.

The Prime Minister has asked me to thank you and your colleagues for taking the trouble to write to her on 17th October about the Inland Revenue computer project.

The ideas you put forward are interesting, but not new. It is, of course, an old adage that 95% of the complexity of any system is needed for only 5% of the cases, although in practice the proportions tend to work out a bit differently. The computer system proposed by the Inland Revenue is intended to deal with the simpler cases within the personal tax system, those coming within PAYE, and the day to day work on those cases will be carried out by clerical staff and their supervisors through terminals in the local offices.

Most people looking at the PAYE project for the first time tend to think in terms of distributed processing using mini or micro processors, but once they grasp the full significance of both the batch processing dimension and the accommodation constraints on putting computer equipment in local offices, the picture begins to change. The plans prepared over the last two years by the Inland Revenue, guided from the outset by substantial external consultancy support, ~~secured by competitive selection from the software industry,~~ have been considered by two independent reviews. In both cases, members were drawn from the systems and software industry. They also considered the implications of distributed processing on the lines you suggest but after detailed consideration endorsed the preferred approach, that is, for an on line system based on terminals in local offices linked to computer centres where the bulk batch processes would be undertaken.

I hope that from this necessarily very brief account, you will be reassured that the current proposals for the computerisation of PAYE are the result of detailed analysis and review and not just a matter of accepting "the proposals of the entrenched interests."

.....



*Gran Pol.*



INLAND REVENUE  
MANAGEMENT DIVISION  
SOMERSET HOUSE

6 November 1980

PS/Chancellor of the Exchequer

COMPUTERISATION OF PAYE : PRIME MINISTER'S QUESTION TIME

I sent you briefing yesterday for PM Question Time on the assumption (valid then) that the Answers to Mr Van Straubenzee and Mr Kaufman would be negative. Since, as you told me, Number 10 decided that the Answers should promise a statement shortly, rather different briefing for PM's Question Time will be needed.

... I therefore attach two lots of briefing, one on the assumption that the Chancellor will be making a statement in the next few days, the other on the assumption that the Prime Minister herself might make the announcement this afternoon, in the terms of the draft Answer already suggested to you for the Chancellor's arranged Question. The latter possibility is perhaps unlikely, but you had better have a form of words to hand in case it is needed.

*Steve Matheson*

STEVE MATHESON

cc PS/Chief Secretary  
PS/Minister of State (Lords)  
Mr Battishill  
Mr Ridley  
~~Mr Springthorpe~~

Sir Lawrence Airey  
Mr Boyd  
Mr Matheson  
Mr Lewis - Press Office



Announcement to be made by  
the Chancellor, on  
Friday 7 or Monday  
10 November.

COMPUTERISATION OF PAYE : PRIME MINISTER'S  
QUESTION TIME

LINE TO TAKE: The Government have been  
considering revised proposals from the  
Inland Revenue for the computerisation of  
PAYE. The Chancellor of the Exchequer will  
be making an announcement very shortly.

SUPPLEMENTARIES

1. Will the business be given to ICL under  
the existing preference policy?

The announcement, when it comes, will deal  
with that.

The Chancellor made clear in his statement on  
8 August, that the Government continues to  
place importance on the maximum feasible  
involvement of UK companies and on ensuring  
a high UK content in the system.

2. Does the Prime Minister agree with the Bow  
Group that the PAYE system should be  
computerised through using very small machines  
rather than big computer centres?

That is a familiar view but it overlooks the  
significance of the batch processing  
dimension and the accommodation constraints



on putting computer equipment into local tax offices.

3. Would not small machines in local offices be a lot cheaper than using big machines?

No. The economies of scale achieved through some centralisation of the big bulk tasks (including printing) which arise in PAYE throughout the year argue convincingly for mainframe machines in computer centres rather than small machines in local offices.

4. Does not the present proposal/going to ICL imply further/unacceptable constraints on Ministerial flexibility/policy options for fiscal change? (The IBM point - Nixon's letter of 30 October to Sir Robert Armstrong).

No. The more gradual implementation now proposed should mean that it would be easier than before to interrupt the process of computerisation (if the delay and cost were thought justifiable) in order to make interim changes.

Opportunities to make major changes (eg self-assessment) must, as before, wait until computerisation is complete.



Prime Minister makes the announcement (on 6 November).

COMPUTERISATION OF PAYE : PRIME MINISTER'S QUESTION TIME

Draft Statement

"The Government have decided to proceed with the computerisation of PAYE on the basis of a simpler, scaled down version of the original scheme and employing a more gradual method of implementation. We consider that this approach will reduce the risks associated with the project, which previously gave rise to concern. On the question of procurement, the Civil Service Department has been instructed to investigate whether terms suitable for single tender can be negotiated with ICL."

SUPPLEMENTARIES

1. Why does the Government not have sufficient information already from ICL to conclude a contract now?

The award of a contract or contracts under the preference policy depends upon satisfactory agreement in terms of price, performance and delivery. Negotiation on these matters cannot and should not be rushed. Detailed discussions with the company have already commenced and an announcement will be made as soon as possible.



2. Does the Prime Minister accept that ICL has the experience and know how to do this job successfully?

The detailed discussions now under way would not be taking place unless the company had the confidence and support of the Government.

3. Why is the Government committing itself yet again to a big, monolithic system using large computers when it would be cheaper and quicker to computerise PAYE through using desk-top business machines? (The Bow Group proposal).

We are convinced that it would be neither quicker nor cheaper to proceed in the way suggested. The Bow Group put in some sound and detailed analysis but they overlook the vital significance of the batch processing dimension to the PAYE requirement and the practical accommodation constraints on putting computer equipment of the kind specified into many of our local tax offices.

4. Why is the Government prepared to freeze the fiscal system for many years ahead by committing to ICL this vast project?

We are not yet committed. As I have already explained, we are discussing with the company



whether satisfactory terms for a contract under the single tender arrangements can be negotiated. There is no question of freezing the fiscal system. The Chancellor will remain free to make normal, annual fiscal changes. More fundamental changes to the personal tax system will need to wait until the computerisation of PAYE is complete. In the meantime, the more gradual implementation now proposed should mean that it would be easier than before to interrupt the process of computerisation (if the delay and costs were thought justifiable) in order to make interim changes.



  
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Econ (80)

PRIME MINISTERComputerisation of Pay-as-You-Earn  
(E(80) 123 and E(80) 124)

## BACKGROUND

When the Committee last considered this issue (E(80) 31st Meeting, Item 1), you concluded that although there was doubt whether ICL could comply with the specification proposed at that time, a less complex system might be adequate for the job, and the specification easier for ICL to meet. Moreover, the centralised system proposed was both more complex, and more vulnerable to industrial action, than was desirable. You invited the Chancellor of the Exchequer to arrange for the design of the computer to be reviewed in time for decisions on tendering to be taken by the end of the year.

2. In E(80) 123 the Chancellor reports that a new scheme has now been devised on the lines suggested by E. He still has doubts about giving the project to ICL on grounds of cost, delay and of technical inferiority. He concludes that "speaking in my Departmental capacity" he could not recommend that we go ahead on that basis. If, nevertheless, a decision is taken to go to ICL on single tender, it will need "to be defended on the broadest grounds of industrial policy".

3. The Lord President's paper (E(80) 124) points to the Attorney General's advice (Annex C of his paper) that, because the procurement of computers will be subject to new EC and GATT rules from the beginning of next year, we shall face grave risks of being frustrated by litigation if we do not complete the contract before the end of this year. Negotiations with ICL would, on this basis, mean a very hurried negotiation, with the risk that the resulting contract does not sufficiently protect the interest of the taxpayer. He presumes that colleagues will, nevertheless, wish ICL to get the contract. If this is the case (and it was the thrust of discussion at the last meeting) the Lord President asked colleagues to note and accept the higher costs and risks inherent in the decision and to authorise a public statement on the lines set out in page 10 of his paper.

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HANDLING

4. You will wish to ask the Chancellor and the Lord President to introduce their papers and then hear the views of the Secretary of State for Industry and the Secretary of State for Employment.

CONCLUSION

5. You will wish to record conclusions on:-

*Int. Standards*

- (i) whether the computerisation of PAYE should now be carried out on the basis of the proposed new system;
- (ii) whether the attempt should be made to negotiate a contract with ICL by way of single tender before the end of the year;
- (iii) what should be said publicly, when, and by whom?

*RA*

(Robert Armstrong)

4th November 1980

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Qa 05172

To: MR LANKESTER

From: J R IBBS

Computerisation of PAYE

1. The revised scheme set out in the Chancellor's paper (E(80)123) is undoubtedly much less risky for an ICL contract than the previous scheme. The CCTA assessment (attached as Annex A to the Lord President's paper E(80)124) supports the view that the project, as revised, is within ICL's technical competence. Because of the more gradual take-on of work and functions, it is probably in any case, regardless of supplier, to be preferred to the earlier scheme.
2. Even with this scheme ICL is likely to cost more than the lowest acceptable tender made in open competition, but one should not put too much weight on the estimated differences between ICL's and alternative suppliers' prices (Annex B of E(80)124). In the absence of a formal open tender they cannot be established with certainty. Once it is decided that ICL should have the contract the important thing is to get the best possible deal from them.
3. There are difficulties in concluding a contract by the end of the year. But these should be surmountable. The pressures on ICL in the negotiations, if the Government plays its hand properly and does not let ICL regard the contract as a certainty, should be no less, and arguably greater, than those on the Government.
4. Moreover, the fact that a contract with ICL has to be signed by the end of the year does not mean that effective checks and disciplines cannot be exercised subsequently. These should include:
  - (a) Making it clear to ICL (both in the contract and otherwise) that a change of supplier would be considered if it were to fail to prove its competence either at the 1981 demonstration of performance, or

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during the initial contract (worth around £2 million) for the test centre and "vanguard" region, or at any time during the subsequent extension of the system (when other manufacturers' terminal and peripheral equipment may in any case be used).

← (b) Requiring ICL to design and build the system to international standards; this would simplify the substitution of another manufacturer's hardware and software for ICL's making it possible to convert at a cost which, when added to another supplier's equipment price, could still be below that charged by ICL to finish the job.

← (c) Ensuring that an experienced and competent software house is effectively included in the development team to supplement ICL's and the Revenue's own resources.

5. We understand that the Revenue and CCTA intend to provide checks on these lines. It is important that they should be effective. If so, they should go a long way to protect the Government's interests and to avert the risk that ICL, having secured the project, might be tempted to exploit its favoured position, e.g. by increasing prices unreasonably or by diverting its most capable people away from the project.

6. I am sending a copy of this minute to Sir Robert Armstrong.

SRJ

4 November 1980





with compliments

Office of the

**PAYMASTER GENERAL**

**68 Whitehall London SW1A 2AT**

**Telephone 01-233-8632**





PRIVY COUNCIL OFFICE  
WHITEHALL, LONDON SW1A 2AT

4 November 1980

The Rt Hon Lord Soames GCMG, GCVO, CH, CBE  
Lord President of the Council  
Civil Service Department  
Old Admiralty Building  
Whitehall  
LONDON SW1A 2AZ

Dear Christopher,

COMPUTERISATION OF PAYE

I have seen your memorandum E(80)124 on the computerisation of PAYE together with the approach set out by the Chancellor of the Exchequer in E(80)123.

I am concerned about the technical assessment carried out by the OCTA as outlined in Annex A to your memorandum. Great reliance is being placed on theoretical calculations carried out by ICL which cannot be confirmed fully until satisfactory completion of demonstrations at the end of 1981. I feel I must draw to colleagues' attention the problems my own office at Crawley is experiencing using established ICL equipment as a warning of possible problems to come with undeveloped equipment.

In November 1979 I was advised that problems were being experienced with my ICL 2900 computers. The original plan was to put in two ICL 2970s but before delivery of the second machine it became obvious that the first machine was not producing the power which ICL anticipated. After negotiations with ICL the second machine was upgraded to a 2976 (Model 1A).

Additional equipment has had to be installed to cope with the shortfall. Negotiations are still continuing with ICL to rectify the problem and apportion cost.

It must be remembered that these problems arose with established equipment with a supposed known capacity. My experience shows that one must treat with some scepticism the estimated output of as yet undeveloped equipment.

I am copying this to other members of E Committee and to the Attorney General.

Yours ever,

ANGUS MAUDE



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Secretary of State for Industry

DEPARTMENT OF INDUSTRY  
 ASHDOWN HOUSE  
 123 VICTORIA STREET  
 LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 3301  
 SWITCHBOARD 01-212 7676

4 November 1980

The Rt Hon Lord Soames, GCMG, GCVO,  
 CH, CBE,  
 Lord President of the Council  
 Civil Service Department  
 Whitehall  
 LONDON  
 SW1A 2AZ

*Jean Christie*

## COMPUTERISATION OF PAYE

Thank you for your letter of 28 October. I note the points you make and I see that they are reflected in your paper for E Committee. We will discuss them further when we meet on Wednesday, but I cannot help remarking now that the picture you present, of officials being unable to defend a procurement decision unless it is for wholly proven equipment without any price differential, seems completely at odds with the way the ICL procurement policy has been implemented in practice, under successive administrations, since 1971.

2. I understand that there have been remarkably few references to Ministers over that period and that officials have indeed taken - and defended before the PAC - many individual decisions which required an interpretation of what was "satisfactory", even if less than the best available, in terms of price, performance or delivery. If officials in a major purchasing Department are now interpreting the openly declared policy of preference for a UK computer supplier so narrowly that they feel the need for Ministerial endorsement at every point, it must raise questions about how they expect to carry through effectively the more broadly based and less formal policies we agreed in February for using public procurement in support of UK industry.

3. That said, I accept entirely that the issues raised by the PAYE computerisation case are ones on which Ministers should decide, not least because of the size and public prominence of the system. I think it is, therefore, all the more important that we should all have a clear and common understanding of the facts before us. There has been far closer collaboration between Departments in the last month or two than there had been before

/our ...

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our previous discussions in E Committee and this is generally reflected in the papers which you and Geoffrey Howe have prepared - though I must note that Geoffrey's current view of ICL's technical abilities seems far more pessimistic than that taken by your own computer experts. On the important issue of price, however, I am not sure that the actual offer made by ICL has been adequately presented in your paper and I should like colleagues to be aware of this point before we meet.

4. My understanding is that ICL have not offered a price of £42 million with a special 20% discount, as might be assumed from your paper, but have proposed an actual price of £33.6 million which represents a standard abatement for a volume order for S3 computers. In addition, they have proposed a standard approach - previously accepted by Government - to the purchase of software (commuting) which would reduce the 10 year cost attributed to them. ICL calculate that this latter reduction would amount to £5.1 million. On this basis (explained in more detail in the annex to this letter), we would actually be paying ICL a total "life cost", over the 10 years, of £68.3 million, as against the £81.8 million you have used as the starting point in your comparisons. We should surely focus on this figure in our discussions.

5. It does, of course, give an entirely different slant to your comparison with what other manufacturers might offer. That comparison must itself be more of an indicator than a firm guide, given the work CSD officials have had to undertake to adjust to a more realistic level the very low quotations put forward by the multinationals. I understand that in the case of IBM it is likely to be on firmest ground, since changes have been made to the assumed IBM offering to take account of the increased power now available from ICL's S3 machine. It is far from clear whether the assumptions for Burroughs, Honeywell and Univac have been adjusted accordingly. However, the different presentation outlined above would put ICL effectively on a par with the costs assumed for IBM and that too seems a major point for us to focus on.

6. I think we should also treat with great caution the idea implicit in your paper, that we could gain further substantial discounts from the multinationals by going to open tender. I have no doubt that they would bend every effort to buy this business in open tender, given its international importance, but that is no reason why we should seek to undermine the position of our own major computer manufacturer when, on both performance and cost grounds, ICL now seems to be able to offer a satisfactory solution to the Inland Revenue's requirement.

7. These aspects of comparative costs seem to me so crucial to our discussion - and to your and Geoffrey's view of whether ICL's proposal is acceptable - that I felt it right to set

/out,...





out my understanding of the position at some length before we meet. I will of course be commenting further on the industrial policy aspects of our decision in Committee on Wednesday.

8. I am sending copies of this letter to the Prime Minister, members of E Committee and Sir Robert Armstrong.

*Yours ever,*

*Kerr*

---





ANNEX

ICL will be announcing their S3 computer (on which their proposal is based) in the course of next week and at the same time they will be revealing both a basic list price and a range of lower unit prices for volume purchases, on a sliding scale. These prices were notified to officials last week, together with a downward revision of the number of computers required (from 50 to 47), to take account of the higher performance now being achieved by the S3. It is on that basis that ICL have proposed a price of £33.6 million for the hardware to meet Inland Revenue's requirement, showing a reduction of 20% as appropriate to an order for 40 or more S3s. But in the price comparison in the Lord President's paper this has been scaled up by 20%, to £42 million, as if the actual ICL price of £33.6 million were a special discount of the kind the multinationals might offer in order to gain this contract. The use, in this comparison, of the price ICL are actually offering would reduce the suggested initial price differential over IBM to zero and the life costs, as presented in Annex B to the paper, to £5.8 million - or 10%.

Even this differential in life costs would be reduced or eliminated if the pricing of software were presented in the manner actually proposed by ICL. ICL offers all customers the option of commuting monthly software charges by a single payment on delivery, with greatly reduced charges thereafter. Government users have taken advantage of this arrangement in the past and ICL have proposed it for the PAYE project. They calculate that it would reduce their discounted software costs by £5.1 million over a ten year period, but this reduction does not appear in Annex B to the paper, possibly because not all the other companies offer a similar arrangement. If ICL's calculation on software costs is correct it would give a life cost, with the new hardware price, of £68.3 million - or only £1.7 million (less than 3%) more than that assumed for IBM.



T. P. Lankester, Esq.



CABINET OFFICE

With the compliments of  
Sir Robert Armstrong KCB, CVO  
*Secretary of the Cabinet*

A handwritten signature in blue ink, appearing to be 'M. J. G.', is written on the right side of the page.

70 Whitehall, London SW1A 2AS  
Telephone: 01-233 8319



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CABINET OFFICE

70 Whitehall, London SW1A 2AS Telephone 01-233 8319

*From the Secretary of the Cabinet: Sir Robert Armstrong KCB, CVO*

Ref. A03432

3rd November, 1980

Inland Revenue Computer

The Chairman and Chief Executive of IBM United Kingdom Ltd. has written to me about the current examination of the various options for a new computer system for the Inland Revenue. You will recall that this question is to be discussed in E on Wednesday, 5th November.

I enclose a copy of Nixon's letter and of my reply. As you will see, I have said that although I cannot enter into any discussion of the points at issue, I will arrange for them to be drawn to the attention of the Ministers concerned. Copies of the correspondence go, therefore, to all Permanent Secretaries of Departments whose Ministers are members of the Economic Strategy Committee (Brian Cubbon, Teddy Youde - in Michael Palliser's absence, Douglas Wass, Peter Carey, Ken Barnes, Brian Hayes, John Garlick, Ken Clucas and Donald Maitland), and also to Jim Nursaw in the Law Officers' Department, since the Attorney General will be attending Wednesday's E discussion, and to Tim Lankester at No. 10.

ROBERT ARMSTRONG

Sir Ian Bancroft, GCB

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cc. Mr. Le Chevalant - for draft reply see.  
Mr. Moore  
Mr. Jbbs.

IBM United Kingdom Limited

Sir Robert Armstrong KCB CVO  
Secretary of the Cabinet  
The Cabinet Office  
70 Whitehall  
London SW1A 2AS

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31 OCT 1980
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PO Box 41  
North Harbour  
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Hampshire  
PO6 3AU  
Telephone: Cosham 321212  
(STD Code 0705)  
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Telegrams: Inbusmac Portsmouth

30 October 1980

Dear Robert,

You will forgive me, I hope, for writing to you direct. I do so with diffidence and with as much detachment as I can muster. You will be able to judge after reading this letter whether I have succeeded in eliminating all bias. I write because I am concerned about the Inland Revenue Computer Project, although I am conscious that I must be seen as someone with more than a passing interest in the outcome.

The main issue as I see it is to strike the right balance between a system which meets the real requirements of the user and providing support for the UK owned manufacturer of computer mainframes. I firmly believe that the single most important criteria by which a successful Data Processing system is judged is the flexible and cost/effective way in which the benefits are obtained. In the particular case of the Inland Revenue, these benefits are:

- The removal of Inland Revenue workload constraints on tax changes.
- The ability to give the Cabinet policy options on major changes to the tax system and structure.
- Savings in staff and costs whilst maintaining the level of service to taxpayers and their employers.

All of these benefits must be achieved in a politically acceptable timescale with a minimum transition period during which the Chancellor of the Exchequer is inhibited from making any but the most modest changes.

It is of very great importance that the Inland Revenue has the ability to choose the best available products to meet these objectives. To suggest otherwise is to remove the discipline of accountability for the results from the Department.

I recognise, and indeed applaud, the Government's wish to maintain a British presence in the important and growing Information Industry of which the computer industry is an integral part. However, I have consistently argued that this objective is better met by Government sponsorship of research and development rather than by preferential procurement which has such potentially damaging consequences.

You may feel that I have said more than enough but if you would like to discuss the matter further, I would welcome that opportunity.

Yours sincerely

E R Nixon

ERN/bw

Chairman and Chief Executive, E R Nixon CBE; Secretary, A F Green

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CABINET OFFICE

70 Whitehall, London SW1A 2AS Telephone 01-233 8319

*From the Secretary of the Cabinet: Sir Robert Armstrong KCB, CVO*

Ref. A03431

3rd November, 1980

Thank you for your letter of 30th October about the Inland Revenue computer.

You will hardly expect me to enter into any discussion of the points raised in your letter, but I can and will arrange for them to be drawn to the attention of the Ministers concerned.

E. R. Nixon, Esq.



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Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

3 November 1980

*ms*

T. Lankester, Esq.,  
No.10, Downing Street

Dear Tim,

Ministers will have seen the references in today's press to the commentary by the Bow Group on the plans for the computerisation of PAYE. Some Ministers may not have seen the pamphlet itself and the Chancellor thought that members of E Committee, to whose private secretaries I am copying this letter, might find it useful before Wednesday's meeting to see the pamphlet and the note attached which deals with some of the issues raised.

The authors of the pamphlet have clearly done a good deal of solid research and some of the points they make reflect those in the minds of Ministers during the last discussion at E Committee of the computerisation of PAYE. Indeed, those led in part to the present revised approach. On the other hand, some of the pamphlet's statements and surmises are pretty wide of the mark, as can be seen from the commentary attached.

Yours ever,

*Richard Tolkien*

R.I. TOLKIEN



DRAFT

THE BOW GROUP PAMPHLET : THE BIG STEAL  
COMMENTARY

Introduction

1. The pamphlet makes some constructive contributions to the debate about the planning and implementation of large Government computer projects. It suggests that the plan for the automation of PAYE is too risky but some of its assumptions are misguided and in several respects the present proposals for the computerisation of PAYE are much nearer to the pamphlet's ideas than the authors could be expected to know.
2. The original Inland Revenue proposals were for 12 computer centres, each of which would be responsible for a large network of local offices. The planned pilot region would itself have been a very large project involving some 2000 terminals and about 2 million taxpayers. Ministers recognised the dangers in what the pamphlet describes as the "Big Bang" approach and as the Chancellor's statement of 8 August made clear, instructed the Inland Revenue to seek a less complex solution. As a result, the revised approach will be to implement the computer system in a more gradual, less risky way and the pilot scheme will cover a much smaller group of local offices.



3. . What the pamphlet does not make clear, however, is the degree of preparatory work which has gone into the present plans for computerising PAYE and the very extensive, relevant earlier practical experience of automation.



Background to the development of the PAYE proposal

4. In January 1978 the Inland Revenue, in accordance with standard government practice, undertook a detailed study of the present requirements. Its main objectives were:-
  - a. to analyse and define the user requirement for PAYE;
  - b. to identify means, if any, by which this requirement could be met using computers;
  - c. to cost justify any alternative solutions and to identify the most cost effective; and
  - d. to produce an operational requirement for the most suitable solution for issue to the trade.

The department recognised that the scope and complexity of this project required technical expertise additional to that available from within the department and supplemented internal resources throughout the exercise by substantial external consultancy support secured by competitive selection from the software industry.



5. In late 1978/early 1979, following detailed definition of the User Requirement, the trade was approached on a broad front; mainframe, mini and micro manufacturers were invited to make proposals for systems to meet the PAYE requirement. Some 46 companies expressed interest and 20 presented proposals. The information in these proposals was taken into consideration in the later stages of the detailed study. Further input from the computer industry was sought in 1979 when two independent reviews were commissioned by CSD and Inland Revenue. Members of both reviews were drawn from the system and software industry. Whilst offering constructive suggestions on various aspects of the Revenue's approach, both reviews endorsed the preferred approach for an on-line system centred on about 12 regional centres. Comments raised by these reviews were taken into account in the final report of the feasibility study, which was presented early in 1980 after two years of detailed work.

6. The report recommended an on-line system for local offices based on 12 regional computer centres, each being responsible for holding the data for the tax offices in a particular region. Regional computer centres were to be connected on-line in a national inter-regional network (not, as the pamphlet claims, a single national database accessed by all regions). That plan seemed to offer the most cost-effective solution for the computerisation of PAYE within a balance between cost, speed of implementation, flexibility and risk.



### Revised Proposals

7. The original proposals for PAYE have been revised at the request of Ministers to reduce technical and implementation risk further. The revised approach will involve a number of independent computer systems, each dealing on-line with a small number of districts. This comes much closer to the Bow Group concept than the earlier proposals. The computers may be geographically co-located in 12 or more buildings but need not otherwise be interconnected. PAYE functions will be introduced more gradually.

### The Bow Group Pamphlet's Proposals

8. The suggestion is that the Inland Revenue should create a MARK I version of the PAYE application through the interaction of two independent groups with the staff of two PAYE districts. The authors of the pamphlet have a strong preference for small business machines with a minimum of mainframes, in what they call 'a distributed solution'. There would be one computer per site, from a very small machine at an isolated district office through larger machines fitted to the sizes of the various conurbations of offices up to a very large machine for the existing concentrations at Bootle and Centre 1. It is claimed that this would reduce the need for purpose-built accommodation, except that the need for a large central index facility for taxpayer tracing is recognised.



## Analysis of Proposals

9. The proposal to create an initial PAYE computer system through a 'trial and error' method is highly risky and of questionable value. Even after the inter-regional network and the more complex on-line functions have been removed, PAYE remains a complex application. The notion of establishing even the most straightforward view of the application in 3 months and then documenting and creating a system in another six is much too optimistic. Even allowing for the possibility of developing a first system within such a time frame, the writers ignore the problems of devising clerical procedures and setting up a supporting organisation and wholly under-estimate the problems of training staff to use the system. The Inland Revenue has responsibility to the public to ensure that the assessment and calculation of tax is carried out as accurately and as expeditiously as possible. The trial and error method has within it the seeds of catastrophe, where a sloppy, hastily constructed system miscalculates taxes on a widespread basis. This would be unacceptable both to government and the public.

## Previous Experience

10. The proposal for a trial and error approach appears to stem from the authors' conviction that the Revenue has little idea of what it wants from a PAYE system.



In fact the PAYE operational requirement represents a logical follow-up to a series of successful system developments over several years. These have provided valuable experience for the present study. Since 1968 the Department has been operating a complete automation of PAYE functions at East Kilbride; this is a batch processing system dealing with about 2.1 million taxpayers. In 1977 a pilot, on-line system for PAYE, named PLANET, was launched in six District offices - covering about 250,000 taxpayers. It provided tax officers with some experience in the use of VDUs for basic PAYE functions and conclusively demonstrated the feasibility and desirability of installing an augmented on-line system throughout the tax service. Although the pamphlet's authors make no reference to PLANET, much of what is to be achieved by their proposed MARK I has already been achieved in PLANET, which has provided over the last three years invaluable information in specifying the requirement of a national system.

#### Comparison with other systems

11. The authors recommend the LACES and CADC computer projects as examples of successful systems. It is noteworthy that neither system was developed using the trial and error method advocated in the paper for PAYE. Indeed government was able to do what is marked as impossible in the pamphlet: to construct a system requirement in detail and proceed to implement it in a gradual manner. The Inland Revenue has adopted the system design



methodology and documentation which proved so effective in the development of the LACES system, and has retained the services of a number of the consultants who were personally involved in the LACES project.

### Summary

12. The pamphlet identifies a number of different solutions:
  - i. One computer per district
  - ii. One computer per site
  - iii. One computer per group of sites
  - iv. A regional solution with 12 computer centres
  - v. A national network linking the 12 regional centres.

The pamphlet's authors prefer ii. The Revenue's original proposal was v, although it has been amended to iv.

13. The claims of the pamphlet's preferred approach, one computer per site, are impressive and look attractive at first sight, but they do not hold up under analysis:--



It is technically simpler. The authors have failed to grasp the batch processing dimension. To achieve economies of scale and be fully cost effective this needs to be organised on a large basis. Batch and on-line work could theoretically be decoupled but the maintenance of two data bases would be complex and time-consuming. Batch processing is likely to become more and not less important as a result of possible future changes in the tax system.

It reduces the communications requirement. Yes, but less than supposed because of the situation described above. Links between the computer centres in the current Revenue approach will be through a simple, off-line process. The pamphlet criticises the concept of 20,000 terminals linked on-line to a single database, but that was never intended. The terminals in the 12 or so Districts linked to a computer will be on-line only to the data base served by that computer.

It uses existing accommodation. The assumptions are wrong. Most tax districts are short of space with no room for the machinery required and could not provide the sort of environment the computers would require.

Maintenance. The pamphlet acknowledges that it would be unwise not to have any trained operating staff at the computer site. The number of sites proposed would increase the need for such staff and exacerbate maintenance problems.

It would allow a computerised system to be implemented much more quickly. The authors claim the system could be fully operational by March 1984. This timescale is unrealistic and risky. The proposed timetable is longer because it includes time to design the full system, program and test it before live operation. The gradual implementation proposed is intended to ensure each stage is working satisfactorily before the next begins.

It is cheaper. The biggest fallacy of all. Distributed processing to the level envisaged would be more expensive than the Revenue proposals.



A CONTRIBUTION TO DISCUSSION ON THE COMPUTERISATION OF  
PAYE ASSESSMENT COMMISSIONED BY THE BOW GROUP:

THE BIG STEAL

(Computerisation of PAYE Assessment)

- AUTHORS :
- John Butcher MP : Worked in the Computer Industry for ten years before election as member of parliament for Coventry SW in May 1979, Vice-Chairman of the All-Party Information Technology Committee and a Director of a Computer Services company.
- Philip Virgo : Organiser of the Parliamentary Computer Forum and author of "Cashing in on the Chips" (CPC May 1979). Worked in the Computer Industry for nine years, including responsibility for planning a number of large scale on-line systems.

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Price: £ 2.50.



Background:

Underneath all the fuss as to who should get what equipment orders there is a growing feeling of unease in the Computer Industry that the stage is being set for another Swansea (the Vehicle Licensing Centre Fiasco); equipment and suppliers will eventually be blamed for the result of decisions taken by a naive and inexperienced user more interested in what is politic (in departmental terms) than in what is practicable.

The Inland Revenue officials involved appear to have been more concerned to seek an alibi against responsibility for failure than to consider what it is practicable to implement in a reasonable time-scale with a limited number of low grade computer staff. After sharp criticism from parts of the British Software Industry, they called in expensive American consultants to back up an unnecessarily complex and grandiose proposal. The consequence was a tender requirement written to dictate an unprecedentedly complex, risky and oversized on-line, networking, database system at considerably greater equipment cost, and many times more accommodation, communications and systems cost, than a basic, reliable mixed system using the experience gained from existing British systems.

Despite the officials eagerness to avoid a subsequent Public Accounts Committee enquiry by taking American advice, they have ignored the lessons of the 175 Reports to Congress by the Comptroller General of the United States, some of which detail wastage and incompetence on a scale which makes Swansea look cost-effective and efficient.

They have also ignored the lessons of the Italian attempt to computerise their tax assessment, using American equipment and expertise, which finally collapsed four years after the start of implementation and had to be rescued by an Italian software house using largely Jananese equipment.

Problems:

The processing requirement is, in computing terms, very straightforward and could actually be met, quite adequately, using anything from 1930's punched card equipment to a few thousand cheap 'home' computers. The fundamental problems are all to do with people.

- \* The high turnover of Civil Service systems staff under a career and salary structure that values technical or managerial competence below political sophistication.
- \* Political inconsistency of the type which halted PAYE computerisation in the mid 1970's because of the possible change to tax credits, subsequently dropped, and may yet cause major changes at short notice.
- \* The probable inability of the Property Services Agency to construct new accommodation, at short notice, even in the middle of a slump in the Construction Industry.
- \* The frequent inability of The Post Office (now British Telecoms) to commission new communications links at reasonable notice, whether to new or existing buildings and the questionable reliability of many links they do commission.



- \* The British paranoia over their tax affairs which will require far higher standards of privacy for this system than, for instance, manually held medical records.
- \* Staff opposition to a system which will be perceived, probably wrongly, to threaten their livelihood.

Recommendations:

The key to successful implementation and development is to get a simple Mark 1 system working in a couple of tax offices as soon as possible, "iron the bugs out" and implement it throughout the country. Then, with the basic data on computer file, and the experience gained from using the system operationally, it will be possible to develop a more sophisticated Mark 2 system to cater for whatever, hopefully more rational, personal tax system the government changes to in its second term of office. The attempt to jump straight to a sophisticated system entails unacceptable risks, given the staff and experience currently available.

The system should be:

- \* Capable of being installed in existing buildings using existing communications facilities or those available at 6 months notice from British Telecoms.
- \* Capable of being operated by existing staff with minimum change or retraining.
- \* At least as secure, rapid and reliable as existing manual systems.
- \* Capable of easy change at no more than 3 months notice for rates and/or allowances or 18 months for a fundamental change, e.g. Tax Credits.
- \* Capable of subsequent evolution into either a decentralised or a centralised network if either proves cost-effective.

All existing staff should receive guarantees of no compulsory redundancy but establishment numbers should not be guaranteed. Staff found surplus to requirements after implementation should be retrained to enable them to move voluntarily to better jobs. The scope for early staff reduction should not be exaggerated, since experience shows that the correction of the many long standing errors and anomalies uncovered when a manual system is computerised can be very labour intensive.

The target dates should be:

1. March 1981 for trial (staff demonstration & evaluation) system(s) working in several tax offices using links to existing government computer installations as necessary.
2. September 1981 trial system(s) to have been amended, in the light of live experience of use for coding and amending returns and assessment for the year 1980/81, and to be ready for wider implementation and trial.



3. July 1982 mark 1 system documented and stabilised for nationwide implementation. Commence study for Mark 2 system in parallel with implementation of Mark 1.
4. March 1984 complete nationwide implementation of Mark 1 system. Issue discussion documents and cost benefit analyses for Mark 2 options.



1. INTRODUCTION : Complex, over-sized and over-sold

1.1 The Salesman's Bonanza:

The concept of 20,000 terminals linked to twelve regional centres has every hardware salesman salivating. The concept of 20,000 terminals communicating on-line with a single database transparently networked over twelve centres has every software guru drooling. Each hastens to assure the officials that he too can do it. No-one questions whether the requirement is necessary or which parts of it (if any) are cost effective. No-one points out that there are few working examples of cost-effective, efficient, large scale, on-line databases, or of large efficient and reliable transparent decentralised networks, let alone of both integrated together, anywhere in the world. If anyone were to do so, and thus by implication question the judgment of the officials, he might well be condemned as naive, backward and uninformed and ruled out of serious consideration for the contract. Suppliers point to small scale applications, limited experiments or simulations and claim that the working reality presents no difficulty. It's like demonstrating a 10 megawatt Nuclear Power Station and saying there will be no difficulty scaling it up to 500 megawatts and installing a dozen, and coupling them tightly together.

Every new bell and whistle added to the system is eagerly praised by the salesmen as they mentally translate it into Order bonus. Unused to the high pressure sales techniques of the multinational computer companies the officials watch, spellbound, as the complexity and scale of the proposals grows in parallel with the praises for their perceptiveness in grasping the potential of this wonderful new tool. Meanwhile ICL, too scared of losing the order to mention that the Emperor has no clothes, is reduced to saying that it too can do just as well, knowing from its past experience at Swansea and elsewhere that, if it gets the order, it will have to pick up the pieces and probably be covered in calumny, while if it doesn't, its reputation in the big systems market will be shredded anyway: "the British Government wouldn't even buy from them a straightforward application like tax assessment so why should you, Mr. Customer.....".



## 1.2 The American Experience:

In March 1977 the Comptroller General of the United States summarised the results of 175 studies in a report to Congress on "Problems found with Government Acquisition and use of Computers from November 1965 to December 1976". The prime problem area was the "Acquisition of data processing equipment without adequate determination of needs", usually leading to the acquisition of unnecessary capacity through:-

- inadequate determination of the scope of the work the computer system was to perform
- failure to make cost/benefit analyses of alternative methods
- failure to consider utilisation of current excess capacity

Examples ranged from the advance purchase of millions of dollars of equipment for a system that had not been demonstrated to work and was ultimately cancelled after 9 years at a cost of \$250 million, (1), to a completely unjustified \$500 million proposal (2). This was followed by a special project which reported to President Carter in April 1979 that "The Federal Government is, in general, mismanaging its information technology resources and has not developed a plan for exploiting the opportunities of the future with respect to investment, service delivery, protection of citizens, or national security ..... apparent unwillingness to exercise managerial control over information technology....abdication....of responsibility for managing information technology as a mission-oriented resource...". That project report contained the information that over 40% of US government procurements were single tender, largely because competitive tender exercise cost more than they saved for contracts of under \$300,000, and tended to lead to protracted delays on major contracts.

More recent Comptroller-General studies have included one on a \$1000 million on-line system which

- " - Is not responsive to national or local level requirements
- Is not reliable
- Lacks economic and effective growth potential
- Cannot transfer data and information effectively " (3)

and a Social Security system which makes erroneous, untraceable, uncontrollable payments of millions of dollars. (4). The titles of two other recent reports say much that is relevant to the PAYE order:-

- 
- (1) United States Air Force Logistics System
  - (2) Department of Agriculture Bureaux Service
  - (3) Worldwide Military Command & Control System
  - (4) Federal Supplemental Security System



- "Data Base Management Systems - Without Careful Planning There Can Be Problems"
- "Conversion: A Costly, Disruptive Process that must be considered when buying Computers"

The former study was undertaken after a number of "Database" systems had proved less cost-effective than the conventional systems they replaced.

The latter study showed that, on average, conversion costs were under-estimated by a factor of ten when they were considered at all, and that, with hindsight, over half the conversions would not have been undertaken.

Before priding ourselves that, with our mature sophisticated software industry and civil service, we manage things better here, we should study the American experience. There are so many parallels in the way we behave that it is clear that the only reason our central government computer blunders have been on a smaller scale is that single-tender procurement has, until recently, protected our commercially inexperienced civil servants who, like their American counterparts, take most computer procurement decisions from high-pressure salesmanship. If the present situation is to end we should read, mark, learn and inwardly digest the Comptroller General's Reports because, page the PAC on Swansea: "You ain't seen nuthin' yet baby".

In particular:

- \* Why does the Inland Revenue want to use a data base management system when US Federal experience, let alone British private sector experience, shows that the claimed benefits are rarely achieved in practice?
- \* Why are they seriously considering buying US equipment which is incompatible with the Tax Collection Systems, the DHSS Social Security Systems and the Department of Employment Systems, let alone the one existing Assessment Centre with which this new system should mesh? U.S. Federal experience is that the overcoming of incompatibility problems can be very expensive.
- \* What are the incremental advantages of the proposed on-line network which outweigh the cost and risk (to privacy and security as well as of disruption), let alone the installation delay that such a complex mesh of communications links will entail and where is the cost/benefit analysis of alternative methods?



### 1.3 The Actual Requirement:

The Inland Revenue employs around 35,000 staff on PAYE Assessment. Each year some 7,000 of these send out and subsequently process 8 million tax returns. (5). The other 16 million PAYE tax payers have their codes calculated using information supplied by employers or gathered in previous years. Allowing for duplicates, the dead and those not currently liable to tax, some 27 million PAYE records are maintained. At the year end about 4½ million adjustments to tax paid in the course of the year are necessary, and these result in about 3¼ million formal assessments. In total the coding process involves some 15,000 staff covering 580 tax districts located in a couple of hundred office buildings. However, many of these staff are concentrated in only a handful of big clerical "factories" such as E. Kilbride (handling 2.1 million taxpayers), Bootle (handling 1.2 million) or Finsbury Square (with 30 districts on one switchboard).

The system is currently structured not according to where the taxpayer lives, nor even according to where he works, but according to where the Inland Revenue staff who handle the tax affairs of his employer are based. Thus a Londoner working in London for a national company whose headquarters are in London may have his PAYE handled in Sunderland. If he then moves job less than a hundred yards to join another London-based national company his tax records may move over a hundred miles to Salford. If the Revenue then decides on a re-allocation of work, without him changing home, job, offices or anything, his tax records may then move a couple of hundred miles to Livingston. Meanwhile, his wife, employed by a small company, may be lucky enough to have all her affairs handled by an office in the local suburban high street. Thus even though the vast majority of the population is geographically very immobile, and rarely moves house or job more than 20 miles, their tax records can regularly move hundreds of miles from one centre of high unemployment to another, resulting in many millions of "inter-regional" enquiries for information. This, questionably necessary, exchange and movement of information appears to account for around 25% of the current workload and was a prime reason for the IR to request an integrated computer network linking all the offices. However, with currently planned rationalisation of procedures it should fall to under 15% and with a return to the geographic organisation of records according to the geographic location of the employer it could almost vanish, except for the occasional exchange of information between adjacent offices covering adjacent districts.

Leaving aside the exchange of information, the average PAYE assessment card is consulted or amended six times a year, with the peak workload in May when as many as 18 transactions per hour per 2,000 records may be reached, compared to the annual average of around half that.

Thus a clerical "factory" like Bootle would generate an average of 4,200 transactions per hour with a peak of 10,400. This may sound an enormous workload to cope with, but is no more than large on-line Public Utility billing systems currently handle on a routine basis. For example, one such utility



with a basic customer record over six times the size of that proposed for PAYE (4,000 characters v. 600) recently logged one of its two ICL 2900 processors averaging well over 4,200 transactions per hour one working afternoon (average response time .64 seconds, no delay over 5 seconds). At the other extreme, the peak load of an office handling a single small to medium size district could easily be handled by a small business computer with half a dozen visual displays and a couple of disc drives costing barely £40,000 in all and taking up no more room than is needed for a desk and, perhaps, a wall-mounted air conditioning unit.

After computerisation the amendments caused by budget, national insurance or building society interest rate changes will be automatically produced by batch computer runs, leaving staff to vet the output and intervene with an overriding terminal transaction only rarely. While it should be possible for a large proportion of the employer-supplied information to be collected on magnetic tape or floppy discs, this pattern may be slow to build up and the entry of deduction card data supplied by employers will initially provide as big a work load as the entry of data from tax returns. The codes would be automatically computed and displayed after such entry and in only a minority of cases would clerical intervention and override be necessary. The time freed would allow more attention to be paid to Assessment, which currently accounts for barely 10% of transactions, and the many miscellaneous transactions such as unemployment repayments or wife's earning elections which account for under 5% of transactions but for most of the public complaints about mistakes and delays.



#### 1.4 The Range of Solutions:

There are many ways to tackle the underlying requirement ranging from a totally centralised system on a single site to a micro-computer on every desk. The five main solutions (given that a single site would be administratively unworkable and a machine on every desk is unnecessary), are:-

##### \* One Micro-computer per Administrative Unit:

Instead of having a bank of filing cards containing the details of about 2,000 taxpayers, each allocation officer and his assistants would have a micro-computer with a screen, a 2 - 5 million character fixed disc (holding the records), a printer and a "floppy disc drive" (for reading or writing data discs for record transfer, archiving, etc.)

The equipment, mounted on a small trolley for plugging into a wall socket adjacent to the desk of whoever is using it, would cost under £5,000 in the volume required so that, adding the cost of a central index-computer (containing information as to which unit currently handles which tax payers), the national cost would be under £60 million.

Except for the central index machine (probably a "Contents Addressable File Store (CAFS) computer, like that being tested by the Post Office for Directory Enquiries), the only accommodation cost would be to check the fuses and earthing of the electricity mains in each office lest any power surge burn out the equipment. Data transfer (including copies to update the central index) would be handled by an overnight mail service for floppy discs, while inter-site enquiries would be handled by a call to the index centre, where the operator would use a screen to interrogate the file to identify where the record is held, followed by a call to the site holding the record.

Tax tables, code changes, programme changes etc. would be distributed on "floppy discs", produced centrally, as for commercial micro-computers or word processors.

Implementation could be very rapid, with no delays for constructions, communications line laying, exchange installation, complex network testing etc.

##### \* One Computer Per Site:

There are a couple of hundred sites housing anything from a single tax district for a few thousand taxpayers to several dozen for a million. A modern British designed and built small business system, like the ICL ME29 Burroughs B90 or Redifon 8000, could support anything from half a dozen screens and ten million characters of storage (for a small, isolated



district) to a hundred screens and a few hundred million characters of storage (for a medium to large site with 50 - 100 thousand taxpayers). Only the handful of big centres, like Bootle or E. Kilbride, would require larger computers with expensive purpose-built accommodation.

Equipment costs would range from under £40,000 for the small office up to £250,000 for the medium to large office, and, allowing for the big centres, one of which would also house the CAFS central index, the total cost would be a little under £50 million.

The main accommodation cost would be wall-mounted dust extraction and air conditioning for sites using exchangeable disc drives (perhaps £10,000 per site), and wiring to connect screens and work stations to the "computer room", which would normally be a conversion of a small office.

The advantages over the "Micro" option are primarily in eliminating the need to pass "data discs" between adjacent districts in the same building or cluster of buildings, and the ability to analyse or manipulate all the records held on the site at one operation (e.g. revising coding notices after a budget change). Though small business systems are normally designed to run without full-time operating staff, it is usually unwise to have no such trained staff available and consequently wait for system support if anything unusual needs to be done.

While there would be cost and organisational advantages in having equipment standardisation, it is not essential. For example, Peterborough Data Processing, whose Unipay system is used to pay 1 in 5 of the working population of Britain, annually alter the systems run on hundreds of their customers' ICL, IBM, Univac and Honeywell computers at only 1 to 2 months notice when tax, national insurance or pension legislation changes with the budget. That operation is much more complex than is likely for PAYE since, while the UNIPAY system is standard, any given manufacturer may have a variety of ranges and some manufacturers have a variety of different operating systems on the same range, each of which can require variations on the UNIPAY programs.

As with the "Micro" solution, implementation could be rapid since only limited accommodation work would be necessary and the systems could be quite straightforward.

\* One Computer Per Group of Sites:

Frequently, a number of small offices are clustered in the suburbs of a city with a large site handling a number of districts in the centre. Sometimes the offices may be only a few hundreds yards from each other. However, the communications facilities available from the Post



Office (now British Telecoms) vary widely from place to place. In some cities the network is reliable and efficient and high capacity lines are available at short notice. In other cities the exchanges are overloaded and traffic vibration has collapsed chambers and concertinaed cables so that it can take years to install a new line and weeks to access an existing line, for repair.

Thus, while it may be theoretically cheaper and more efficient to group adjacent offices, such grouping should be dictated more by the services available in practice from British Telecoms rather than distance. Such grouping would save several million pounds over the previous option and would often remove the need to physically transfer data between offices serving neighbouring towns or suburbs. Implementation would be delayed by as long a delay in line availability as is deemed acceptable rather than have an additional computer. The additional accommodation work for communications equipment is, by comparison, negligible.

\* Regional Centres:

Theoretically, the cheapest solution, at a cost of around £36 million, is to provide 12 centres servicing one workstation per 2,000 tax records, sited in local tax offices for on-line entry and validation of data and enquiry purposes. However, at least as much expense again is likely to be required for the construction of purpose-built accommodation, since only rarely is existing accommodation likely to be adequate.

The delay while communications links are installed could be considerable in four of the cities being considered for such centres, while the subsequent vulnerability to disruption also needs consideration.

Moreover, some regions have little geographic cohesion and any attempt to centralise, for example, Eastern Counties on Peterborough, could prove as problematical as the attempt to centralise the computing of the Anglian Water Authority on Huntingdon.

\* A National Network:

This is the salesman-favoured option with communications processors and many more workstations added to the regional centres of the last option. Its main advantage is the easy transfer of data anywhere in the country. Its disadvantages spring from its complexity and consequent vulnerability. Reliable implementation cannot be tested until the last site is commissioned since traffic on a decentralised network rises exponentially with the number of sites linked and a network adequate for 11 sites could be swamped by the 12th. Therefore, it is easily the longest to implement and the most vulnerable to construction or communications delay.



(A centrally controlled network would be easier to implement but subsequently more vulnerable to disruption).

The vulnerability to illicit access will dictate rigorous security which will, in the nature of security systems, inhibit, delay and increase the cost of legitimate access.

It is also likely to be the most expensive since, in addition to the £30 million for the centres and £30 million for the network concentrators and workstations must be added the purpose-built accommodation and high capacity landlines on a greater scale than for the stand-alone regional centres.



## 2. THE REAL PROBLEMS:

Technically, none of the possible solutions is more complex than a number of existing UK Public Sector systems already running on British Equipment. There are even multi-centre national networks, though the additional cost and effort of linking the centres has rarely been justified in practice, and at least one is likely to be scrapped in the near future (along with the centralisation plans of its late management). The main problems are managerial, given a user with a salary and career structure which inhibits the retention of skilled computer staff and frequently rewards according to seniority or the number of subordinates rather than the job done. Lesser problems, significant according to the chosen technical solution, are to do with communications and security.

### 2.1 Staff Competence:

Discussion to date has largely been a one-direction mud-slinging match against one supplier. Belatedly, the competence of the mud-slingers is also coming into question as the stories of the Italian Tax Computerisation, the US Social Security System, the USAF Logistics System, WWMCCS, the St. Louis Federal Computer Bureau, etc., emerge to dwarf the Swansea fiasco.

However, as Swansea showed, the most critical factor is the competence of the staff who are to assess, implement, maintain and administer the chosen system. By comparison, the competence of the supplier is almost irrelevant.

The suppliers did not program the computer systems of the UK banks or of the Airlines. They did not supply most of the networking software or expertise. They do not even maintain many of the most critical items of equipment.

The banks trained their own staff over long periods of time, they retained consultants (sometimes on permanent contract), they poached staff from the Post Office, they bought staff on the open market. Maintenance, and rapid repair, is more important than the original design and installation. The competence and integrity of the staff who maintain the networks is critical to the profitability of the organisation. The staff are rewarded accordingly. Some are paid more than the top of the Permanent Secretary's scale.

It is folly to plan for a system which is critically dependent on this type of staff without recognising that to recruit and retain them is incompatible with the current civil service hierarchy and salary structure. The civil service is chronically short of competent computer staff of all kinds and union pressure blocks the use of contract staff except for short duration projects of a nature where permanent staffing on location is clearly inappropriate.

"You can't get there from here". The staff necessary to run the type of network envisaged cannot be hired from outside on current civil service salaries. They cannot be trained from inside in the time available and, even if they could, would more than



double their earnings on leaving. On a project of this size and visibility the civil service unions would firmly oppose the use of contract staff on other than a temporary basis.

In the long term the answer to the staff problem lies in changing the status of computer staff within the civil service hierarchy so that two-year assignments on programming and system analysis (non-consecutive) are part of the career progression of every Administrative/HEO Trainee. The integration of computing into the mainstream of the service would break the log-jam on the other changes needed. Though barely a handful of programmers would carry a Permanent Secretary's baton in their knapsack, the possibility of promotion to the Administrative Grade would greatly change attitudes.

In the timescale of this project, however, the effective options are far more limited. Either:

- \* Limit aspirations to what can be achieved with the current, largely low-grade, high-turnover computer staff.
- \* Subcontract not only system development but also operations and maintenance, as with the highly successful LACES (London Airport Cargo Documentation) or CADC (Computer Aided Design Centre) operations.

If the operation is to be based on Regional Centres, with or without a national network, there is no hope of developing the necessary in-house expertise to operate and maintain the system in the timescale available. If the Police National Computer Centre rates of pay are inadequate to hold the expert staff necessary to restore service rapidly after, or to prevent, periodic network crashes, then the Inland Revenue does not stand a chance and should not try.

Subcontracting is not cheap. It will cause problems with the civil service unions whose own members are denied the higher rates of pay. But it is the only way to make a centralised system work.

The alternative is to limit aspirations to a simpler, distributed system. The skills necessary to program or operate small business computers serving a single site are well within the grasp of most of the Inland Revenue's current staff, given adequate training. Not only can existing computer staff handle such equipment but their ranks can also be readily topped up with staff found surplus to requirements in the course of the implementation who are also found to have an aptitude for, and interest in, this type of work.

Moreover, the initial development of a system for such equipment can be very much more simple and rapid and the installation of such equipment and implementation of systems is very much simpler. It is the kind of task that the major computing companies frequently give to their second-year graduate trainees.



## 2.2 Redundancies:

The highly ambitious proposal for a sophisticated computer network has been said to have originated in the desire to put implementation off until the current recession is over and thus avoid widespread staff opposition. Certainly, the Inland Revenue staff association is determined in its opposition to any cut in establishment, let alone redundancies. That many of the jobs they wish to keep are dispiriting and soul-destroying, fit only for automata, appears to be of less importance. One suspects that the motivation for the campaign comes more from the management, with headcount related pay, and the union organisers, with an eye on subscription income, rather than from the rank and file, more interested in a "no compulsory redundancy" guarantee for themselves and a better life for their children.

A distributed solution with early implementation on pilot sites and thus early visible redundancies could result in massive union opposition to standardisation on the chosen system. However, that opposition is likely to come anyway, whether forewarned by pilot schemes or not. Far better to pre-empt it with "no compulsory redundancy" guarantees as the Post Office has done with System 'X', and a selection of pilot sites for smooth implementation in areas where high turnover makes staff retention the problem. In the areas of low unemployment, staff wastage will allow rapid savings and any remaining staff can be upgraded in reward for their co-operation and increased productivity without increasing costs. Such visible rewards and improved working conditions should serve to sweeten the reception elsewhere even though the lack of staff savings in areas of high unemployment could make improved working conditions the only tangible reward.

The risks and cost of labour disruption also make this a key area for a first attempt to introduce a policy of "no strike" guarantees in return for protected conditions.



### 2.3 Communications:

With distributed processing systems the problem is to keep the various systems in step. With regional centres or a national network the problem is to maintain the communications links. Theory favours the latter; experience frequently favours the former. One of the reasons for the discrepancy is that traffic, particularly heavy lorries, is shaking apart the underground telecommunications transmission system in many of our city centres. In parts of West London where the access chambers have collapsed it can take two weeks of digging to get to a simple fault that should have been a two hour job from callout to clearance. In one major city, the access chambers and ducts have been maintained, at considerable expense, but adjacent gas mains have fractured and extractor fans may have to be run for 24 to 48 hours before it is safe to send down staff with equipment that might cause a spark. Under one-way road systems older cables "creep" with the vibration, stretching at one end, concertina-ing up into the access chambers at the other end. Thus when faults develop in the stretched section the road may have to be dug up to correct them and the cable relaid.

In short, while the Post Office is worrying about possible job-loss in the future when it gets round to replacing its antiquated exchanges, road traffic may be smashing up the transmission system which serves them, creating a massive backlog of work to be done now.

The consequence for many computer installations hoping to make extensive use of communications facilities, is that unless they are sited where the Post Office can serve them with overhead facilities (including microwave), or with underground facilities beneath lightly used or well constructed roads, connection delays can be considerable and subsequent reliability questionable, even if the exchange lines are available.

This situation dictates that, if PAYE is to be computerised over a relatively short space of time, the less reliance placed on Telecommunications facilities the better. The inability of the Post Office to expand its own packet-switching service to meet existing demand from existing customers, let alone add new customers, is yet another example of the problem. Whether it is solved by satellite communications and roof-top aerials or by making heavy lorries pay for the damage they cause with realistic licence fees, the problem will be with us for many years.

A common, private enterprise solution is to hire a Post Office engineer with a knowledge of the network round the proposed installation and extensive personal contacts so that planning can take place on a realistic basis and the bureaucratic hierarchy can be bypassed. Thus, instead of being told by a senior administrator that the delay on PABX extensions in North London is 18 months when you request another 100 lines, the maintenance engineer on his "weekly visit" may be able to remove a resistor or two to link in the 100 spare lines that were included when the installation was first put in, and arrange the necessary paperwork to follow. The key is to know what questions to ask, of whom,



so that early planning - e.g. siting the switchboard on this or that side of the main road on a split site, can be done in full co-operation and that, subsequently, realistic levels of service are agreed and maintained.

For the civil service the cost and the precedents of poaching a couple of practicing Post Office engineers per region and then arranging a service via the back door may well not be practicable. If so, the built-in bureaucratic delays or working through the official channels could well add 18 months to 2 years to the provision of any given facility plus additional expense at all levels.



## 2.4 Security:

In Britain, even more than in other countries, we are paranoid about the privacy of our tax affairs. Computer systems can, at the same time, greatly improve and greatly threaten that privacy. Without password and user number it is almost impossible to extract information from a modern computer system while a man in a doctor's white coat or engineer's overalls with an easily forged identity card can usually gain access to most manually held files in any large organisation from hospital to factory. However, many clerks write their passwords in diaries or on labels stuck to their workstations and rarely change them. Thus it is often easy for a casual visitor to note and remember the password for subsequent use, from a terminal tapped into a private line or even (in the case of a \$12 million dollar bank fraud) from a telephone kiosk.

This would present little problem in the case of a computer system accessible only from within a single building, or group of buildings, with terminals locked when not in use. However, when outside terminals are in use over dial-up lines, or even over private tie-lines, the problems can be enormous. Unless the terminal identification and password are encrypted, the eavesdropper tapping the links to the regional centre can subsequently call in with his terminal even though all the clerical staff adhered to strict privacy rules while, without total encryption of traffic, he could tap all transmissions.

To guard against such eavesdropping by use of on-line encryption would increase the costs of the local workstations quite sharply while the risk of lax security over passwords is likely to be insurmountable in practice. Thus, if security is seen as particularly important, restriction of the access points by restriction of the transmission and communications network is essential.



### 3. IMPLEMENTATION & DEVELOPMENT : IT'S NEVER RIGHT FIRST TIME:

#### 3.1 The Recommended Approach:

Given the prime objective of the successful implementation in a reasonable timescale, of a cost-effective system capable of subsequently facilitating radical changes to the tax system, the key to a practicable approach is flexibility. The system must use existing staff, buildings and communications as much as possible while retaining the capability of subsequent growth into either a centralised or a decentralised network as changes in organisation, tax structure, communications facilities or technology make this economic and/or desirable.

Therefore we recommend a solution based primarily on small business computers for each site using shared larger machines only where existing accommodation and reliable communications links make installation in a short timescale relatively easy.

This also reduces the vulnerability of the operation to disruption from whatever cause.

We also recommend that the initial system be straightforward and robust enough for currently available computer staff to develop and implement nationally, and user staff to learn to operate, before the end of this government's first term of office.



There are three main approaches to system design and implementation:-

- \* Big-bang - Rebuild the Universe
- \* Delayed Big-bang - Plan very carefully for four or five years then rebuild the Universe to a precise specification
- \* Evolution - Piecemeal step by step improvement within an overall strategy but without total initial commitment

The "Big-bang" approach has led to too many expensive fiascos to retain any credibility. Most computer companies have switched to an evolutionary process for their internal computer systems and for package or operating system development, but do not recommend it to their customers because it gives little opportunity for spectacular, promotion-earning sales campaigns. Thus we have the popularity of "Delayed Big-bang"; also known as "Bay of Pigs" because the CIA spent many years planning that operation in meticulous, secretive detail before going ahead. This approach gives many opportunities for lucrative consultancy business and evaluation exercises with much enjoyable intellectual exercise and wining and dining plus the near certainty that the "high-flyers" will have flown on before implementation is due and the chickens come home to roost.

"Delayed Big-bang" is based on the false premise that, given enough study, one can design a fully workable and stable system to meet user requirements in a cost-effective manner. The reality is that hardly any users know what they want in sufficient detail to do a sensible specification and, if they do, wouldn't have wanted it at the resulting cost. However, presented with trial systems and a responsive computer department, most users can quickly sort out, from the options offered, what they don't want, what they can afford, and what they are prepared to pay for. After a few months of use their views will have changed, some functions will be redundant, others would be useful. Usually, the useful ones are cheap to provide while the "nice but not really necessary" are often prohibitively expensive (though the salesman loves them and always tried to sell them to the Board). After a year or so the system can be "stabilised", re-written for more efficient use of computer resources and easier maintenance and documented. This process is "Evolution". Usually the computer department has a clear strategy as to how the system is to be developed but each stage is cost justified with full user acceptance before the next one is committed.

Under this approach, documentation, testing and training procedures are not commonly drawn up until after the system has been frozen. Since these are much the most time consuming and labour intensive activities in system development, it is commonplace for the trial systems to be up and running within ten to twelve weeks of the assignment of staff.

Given the lack of practical computer experience that most Inland Revenue users will have, it is almost certain that the first system to be developed will contain many flaws. It is also unlikely that the second will be perfect. Most public utilities have gone through three or four billing systems making fewer mistakes each time. Therefore, it is particularly important for the Inland Revenue to follow the evolutionary path rather than the expensive delay, and possibly disastrous future commitment, of the consultancy-studied "Delayed Big-bang".



### 3.2 Trial and Error:

The first step should be to set up two or more development teams. Each team should consist of a couple of user staff, a couple of systems analysts and a couple of programmers. Using either terminal facilities to existing computer installations or rapidly installed small business systems, each team would be allocated a district of around 10,000 taxpayers with the objective of having a system operational for March 1981. The districts selected should be fairly straightforward, without major staff problems, and include at least one rural and one urban location. Which functions the systems handle and how they handle them would be up to the teams and the local tax office staff with whom they deal. It would be up to the teams how much use they chose to make of manufacturers or consultancies services, within a budget of no more than £50,000 per team. It would be up to the teams whether they chose to collaborate or compete in the period to March 1981.

Given the amount of prior study and preparation that has already been done, a rapid decision could allow this timescale to be shortened. However, given that this approach is new to most Central Government computer staff, it is unlikely that the commercial standard of 3 elapsed months from assignment to working trial system can be improved on. It should also be made clear that this this approach relies on documentation and specification being done after the system is stabilised.

From March 1981 to September 1981 the teams should exchange experiences and develop their systems, using experience gained in the coding of returns and preparation of assessments in the 1981 "tax season" from March to June. Over this period preliminary assessments of the various approaches could be made and additional equipment installed to expand or duplicate some of the more promising systems.

From September 1981 to July 1982 the amended systems, less any shown to have no future, should undergo a full operational trial. Development would be permissible in this period since the trial would be of the cost-effective service to the users and a system which could sustain this while simultaneously being developed would be demonstrating an admirable evolutionary capability and robustness.

In the course of this trial the plans for phased installation of equipment to support any of the systems under trial would be prepared and orders placed. Evaluation would take place throughout the trial together with the cross-fertilisation of facilities between the systems under trial so that by July 1982 all would be ready for implementation nationwide to take place. It could be that different systems are found suitable for different types of office. It could be that equipment from different manufacturers is found suitable for different environments. So long as information can be cost-effectively transferred between districts without a clash of formats and standards which leads to expensive delay or confusion, standardisation need not be paramount. British Caledonian uses computers from ICL, Univac, Itel (an IBM compatible supplier), Raytheon, Wang, Data General and Jacquard, and is not thought to be markedly inefficient, though such a plethora of suppliers is unusual and American government experience would place



a greater value on compatability and continuity from a single supplier than the often illusory advantages of competition.

Therefore, while the development teams need not necessarily use identical equipment for their trial systems, they should use compatible equipment. The added cost and complexity of developing machine-portable facilities could inhibit the cross-fertilisation which is such an important feature of this approach, so that there are further advantages in an early decision on equipment or manufacturer standardisation.



### 3.3 Phased Implementation:

From July 1982 onwards geographically based teams should help each site in turn to install its equipment and then each district, in turn, to switch from manual to on-line working. Until implementation is complete each computerised district may need to transfer or receive data on paper, as opposed to computer media, when dealing with non-computerised sites.

Where a single computer is to support a number of districts in the same building and a number of districts in other buildings, linked by telephone lines, one team should handle the equipment installation, beginning centrally and then working round the outlying offices, while a second team should follow, instructing in the use of the system, training, and providing an advice and guidance service to the users for up to a year after implementation.

The implementation teams will have been selected and trained in the parallel with the one year operational trial, probably from staff involved in that trial, including staff from the development teams. Assuming that by July 1982 the trial system(s) are operational on a dozen sites serving two dozen tax districts that will leave around 550 districts on a couple of hundred sites still to be converted. The equipment installation is unlikely to require more than a fortnight from a 2 or 3 man team to check wiring and installation on most sites, to supervise the local staff for their first week of operation, and provide a back-up service for three months. The 3 to 4 man "instruction" teams, by contrast, may need up to three months to train the allocation officers and clerical assistants in the use of the new system and to supervise/assist the initial loading of data and early use of facilities. Thus only half-a-dozen equipment installation teams but perhaps 50 "instruction" teams are likely to be needed. Since the implementation teams will need to have a full understanding of the operations of the tax system and 150 - 200 staff is a lot to spare, it is particularly important that the early trial systems are installed in areas where alternative employment prospects create high morale and thus surplus staff will accept assignment to the implementation teams and the prospects of mobility and a markedly more varied career path thereafter.



### 3.4 Flexible Evolution:

The simpler the trial systems the easier their implementation. However, implementation of the Mark 1 systems should only be the first step on the path to a more equitable tax system. Even while implementation is proceeding, the teams involved should be considering the practicability of the possible radical changes in organisation and principle that computerisation should make possible. If the initial system is based on local sites using communications facilities where readily available, but not waiting if they are not, and certainly not waiting for cumbersome networks or major construction works, a far greater degree of flexibility will be available much sooner.

Whether that flexibility is used to introduce local Income Tax, Tax Credits, Wealth Tax or merely to identify and remove inequitable and uneconomic discriminations cannot be reasonably predicted in advance. In consequence any attempt to build detailed assumptions into the Mark 1 system for "structured flexibility" is likely to be doomed. The fallacy that better planning will allow for the unpredictable, which is at the heart of the database myth, should not be allowed to delay the achievement of that flexibility. The greatest planning exercise of modern times, the Invasion of Normandy, was thrown away on Day 2 when a storm wrecked the beach-head. But by then it had achieved the objective and the men and materials were available, even though the elaborate follow through timetables, on which so much time had been lavished, were so much waste paper.

Once the staff are relieved of laborious manual manipulations, whether the files are on one computer or two hundred, the way is open for change. Change on two hundred semi-independent systems can be easier to manage than on one interlinked network since, while it is harder to keep them in step, it is nowhere near as necessary to do so. Thus, while a tax credit system or local income tax system would need to come into force overnight, the preparation for that system could be more easily phased over a few months with a decentralised computer organisation. Similarly, the heart of the ability of the "Payroll" service companies to change the programs run on hundreds of computers with a 1 - 2 month window at budget time is based on neither communications networks nor database systems, but on "Securicor and structured programming". Both in use for over 20 years and still more reliable.

A centralised, or at least centrally co-ordinated, network should not be ruled out as a future possibility. However, by the time the telecommunications network of Britain is capable of supporting a comprehensive, nationwide "star" network of the type currently envisaged, the availability of microwave or satellite based "ring" networking facilities will probably provide a much cheaper alternative. Therefore, the possibility of a future network, overlaying the equipment installed for the "Mark 1" solution, should not delay or dictate the shape of the interim solution.



#### 4. ACTION PLAN

##### 4.1 Immediate:

- Set up two or more development teams with the objective of demonstrating working on-line systems serving named tax districts in March 1981.
- Order enhancements to existing computer equipment and/or two or more small business systems for delivery by December 1980 to support the above demonstration(s).

##### 4.2 By Christmas 1980:

- Order a dozen small business systems and/or enhancements to existing computer mainframes for delivery July to September 1981 for expansion and full trial of the development systems.
- Order a large mainframe, capable of supporting a central CAFS style index service and/or a major centre (e.g. Finsbury Square or Bootle) with or without communications links to outside sites.
- Commence a study of communications facilities currently available from British Telecoms to determine which existing sites, if any, can be used to support terminal networks in outlying offices over lines and links likely to be available over the period to December 1983. This study should include the dates facilities could be made available to any given site to enable implementation scheduling.
- Place outline orders/letters of intent for sufficient small business systems processors, mainframe processors, work stations and disc storage to support systems in those sites that are almost certain to require them. These orders should include outline schedules of delivery, bulk discounts for phased delivery over a long period, and penalty clauses for major variations.
- Place outline orders for work stations for those sites where it is not immediately clear whether terminal links or local processors will provide the service.

##### 4.3 March 1981:

- Commence evaluation of trial systems.
- Complete study of communications facilities.
- Nominate sites and districts for the September 1981 to July 1982 operational trials, commence any site preparation, commence appointment of operational trial teams.



4.4 By September 1981:

- Consolidate and document trial system(s), using pooled experience, for operational trial.
- Install equipment for operational trials.
- Appoint operational trial teams.
- Confirm which sites are to have processors and which to be served by communications links.
- Confirm schedule of communications requirements to British Telecoms.
- Place outline orders for processors, enhancements and discs where requirements had previously been uncertain.
- Commence confirmation of the details of previous outline orders.
- Commence installation of "Index" centre.

4.5 By July 1982:

- Consolidate Mark 1 system.
- Appoint and Train Implementation and Instruction Teams.
- Confirm details of all equipment orders and schedules.

4.6 By Christmas 1983:

- All processors to be installed, final round of implementations under way.
- Cost benefit analysis for Mark 2 system options under way.

4.7 By March 1984:

- Mark 1 system fully operational nationwide.
- Cost benefit analyses and discussion papers for Mark 2 system issued.



B I B L I O G R A P H Y

Problems Found With Government Acquisition and Use of Computers from  
November 1965 to December 1976.

FGMSD-77-14            March 15th, 1977.

Federal Data Processing Reorganisation Project.

Summary :	PB-294-543	April 1979
Acquisition Team Report	PB-283-757	June 1978

Flaws in Controls Over the Supplemental Security Income Computerised System  
Cause Millions in Erroneous Payments.

HRD-79-104            August 9th, 1979

The W.W.M.C. & C.S. - Major Changes Needed in Its Automated Data Processing  
Management and Direction.

LCD-80-82            December 14th, 1979

Data Base Management Systems - Without Careful Planning There Can Be  
Problems.

FGMSD-79-35            June 29th, 1979

Conversion: A Costly Disruptive Process That Must Be Considered When  
Buying Computers.

FGMSD-80-35            June 3rd, 1980

PAYE - Possible Future Developments.

Somerset House        March 1979

London Telephone Directory



cc: Chief Secretary  
Financial Secretary  
Minister of State C  
D Wass  
Mr Battishill  
Mr Dixon  
Mr Unwin  
Mr Gordon  
Mr Ridley  
PS/Inland Revenue



part

Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

28 October 1980

The Rt. Hon. James Prior, M.P.,  
Secretary of State for Employment

E H M

COMPUTERISATION OF PAYE

R

Thank you for your letter of 7 October, on which John Nott and Christopher Soames have commented and to which the Prime Minister has also reacted.

I understand your concern that all the work on the review set in motion by E Committee on 7 August should be completed in good time for a decision and for conclusion of single tender arrangements by the end of this year and I note what you and colleagues say about deciding in favour of ICL. As Christopher said in his letter of 13 October, however, there are still some difficult matters to resolve before that decision can be taken. He is about to circulate a paper for E Committee (to be taken on 5 November) dealing with the EEC/GATT problem and with the difficulty that the ICL proposals are likely to be significantly more expensive than those of the company's major competitors.

My own concern is not limited to the fact that we will be paying a lot more money to buy an inferior system which will show smaller savings, important though these considerations are. I have in addition particular reservations about the potential difficulty and delay during the development and implementation of the system. My paper for E Committee will describe the way in which the plans for the PAYE project have been revised to ensure that we could have greater confidence in ICL's ability to do the job than we had under the original proposals and will say that, subject to the agreement of colleagues that the current reservations are not sufficient to preclude a single tender decision, we shall do our best to make an ICL solution work. But the timetable will be uncertain.

Under the original ICL proposals, we were worried about the possible prolongation of the design and development period required for the system, with additional costs and deferred savings; by the prospect of the development of hardware and software continuing into the period when the computer system was being designed; and by the unquantifiable risk

/of excessive



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cc: Chief Secretary  
Financial Secretary  
Minister of State C  
D Wass  
Mr Battishill  
Mr Dixon  
Mr Unwin  
Mr Gordon  
Mr Ridley  
PS/Inland Revenue



purf

Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

28 October 1980

The Rt. Hon. James Prior, M.P.,  
Secretary of State for Employment

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R.

COMPUTERISATION OF PAYE

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/of excessive

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of excessive systems failures if the new equipment proved to be unreliable. Prima facie those fears are lessened if the technical requirement is made less complex in order to fit ICL's capacity, but they are not removed. The development of the combined on-line and batch computer system for PAYE remains a considerable task and the basic equipment proposed by ICL to do the job, its S3 computer, has not yet completed its development or been tested in relation to the other new equipment proposed by ICL to meet the PAYE requirement. We do not yet know how big a workload it can reasonably sustain or how reliable their solution will prove in practice. While we can insist on very comprehensive demonstrations next year, before the final contractual details are agreed, the reliability of the new system will not be demonstrable until it is subjected to the stress of live operations. There is much that could go wrong, and the potential for delay remains high.

In planning the revised approach and in calculating costs and savings we have assumed a start on a more limited approach by the end of 1983 with completion of that phase nationwide by the end of 1987. The CCTA's advice in relation to the original project was that a single tender commitment to ICL could add at least a year to the development timetable. Under the more evolutionary approach now proposed they take the view that implementation should be more manageable and that the danger of such delay should be reduced but would not be removed. We just do not know. There must therefore be serious reservations about any firm commitment to dates for start or finish of the project if we proceed by single tender. The Revenue and CCTA team will need to liaise very closely indeed with ICL in order to monitor performance in development and provide us with progress reports, possibly on a quarterly basis, as the project proceeds. They may well require extra resources to cope with that.

GEOFFREY HOWE

A handwritten signature in dark ink, appearing to be "G. Howe", written over a horizontal line.

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RESTRICTED



Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

The Rt Hon Sir Keith Joseph, Bt, MP  
Secretary of State for Industry  
Ashdown House  
123 Victoria Street  
LONDON SW1E 6RB

*I hope this will refer us soon come any reference*  
28 October 1980

Dear Keith,

*in the letter by the department for decision*  
*MS*  
*(2)*  
*R 28/10*

COMPUTERISATION OF PAYE

Thank you for your letter of 21 October. As you say, we shall return to these questions in E Committee.

But I must make one point now. You say that it must be possible for officials to find a way of implementing a decision to give the contract to ICL under our current procurement policy without real risk of legal challenge or PAC criticism.

I must tell you straight away that I think this is highly unlikely. We can look to them to give us the most accurate facts and figures they can, but it will be essentially for Ministers both to take the decision and defend it. The current policy stipulates that ICL shall receive major contracts subject to satisfactory price, performance and delivery. As regards price, I am told that there is likely to be a very considerable discrepancy, with ICL being uncomfortably higher than competitors. Then they are proposing to meet the requirement with a new computer whose performance has not yet been demonstrated.

It is open to us to decide that we should incur a certain price differential and contract to buy unproven equipment. We may do so. But if so, we must then also decide how we wish to present the decision. What we should not do, especially in the light of the assurances which have been given to the Public Accounts Committee, is to leave it to officials to defend such decisions as fully consistent with the existing policy. It is not for them to say that an excess of a particular percentage is a satisfactory outcome; how could they? As I say, these are matters on which we will have both to take and defend our own decisions.

Copies of this letter go to the recipients of yours.

*Yours ever*  
*Christopher*



Civil Service Department,  
Whitehall,  
London, SW1A 2AZ

*With the Compliments*  
*of the*  
*Lord President of the Council*





Civil Service Department  
 Whitehall London SW1A 2AZ  
 01-273 4400

*M. Patten*

The Rt Hon Michael Heseltine, MP  
 Secretary of State for the Environment  
 2 Marsham Street  
 LONDON SW1P 3EB

27 October 1980 *MSM?*

Dear Michael,

*Not copied to No 10. Will request if required. <sup>27/10</sup>*

I have seen your letter of 26 September to John Biffen and his reply of 7 October.

I have already written about the PAYE project (my letter of 13 October to Geoffrey Howe). This letter concerns the question of computer accommodation for my own department at Chessington. As you will know from Paul Channon's letter of 25 September, we were glad to see that provision had been made for this in the programme for new starts in 1981-82. It is a small (£200,000) but very important project which is vital to the programme for replacing the Chessington computer, on which the pay of 100,000 civil servants depends, as does the development of the standard payroll system for use by other Departments.

In order to keep to the replacement timetable we must be in a position to make a contractual commitment to ICL very soon but clearly this cannot be done unless it is certain that the necessary modifications to the computer accommodation will be made in time for it to receive new equipment. I would be glad therefore to have your reassurance that provision for this small but essential project will remain in your modified programme for 1981-82.

More generally, Paul Channon has already expressed serious concern to you and Geoffrey Howe about the effect of cuts in PSA expenditure on schemes to reduce overcrowding and improve working conditions. These are not designed to pamper civil servants but to improve deplorable conditions in local offices. Sir Derek Rayner has commented strongly on the poor conditions in which some staff work at local level and on the adverse effects that these conditions have on the loyalty, efficiency and morale of staff, as well as the wasteful costs that they engender. Many of the



improvements are already long overdue and I am becoming very concerned about the effect that further delays will have on staff morale. I must press for the retention of as many of the schemes as possible in the 1981-82 OGA programme.

Copies of this letter go to other members of the Cabinet including the Minister of Transport and to Sir Robert Armstrong.

Yours ever  
Christopher

SOAMES



file

Econ Pd

BE s/n/80

22 October 1980

The Prime Minister is interested  
in the thoughts about the Inland Revenue  
computer set out in the enclosed letter.

17.10.80

I should be grateful if you could  
let me have a draft Private Secretary  
reply by 5 November.

M A PATTISON

Richard Tolkien, Esq.,  
HM Treasury

MAM



cc A. Dignid

2



DEPARTMENT OF INDUSTRY  
 ASHDOWN HOUSE  
 123 VICTORIA STREET  
 LONDON SW1E 6RB  
 TELEPHONE DIRECT LINE 01-212 3301  
 SWITCHBOARD 01-212 7676

Secretary of State for Industry

21. October 1980

The Rt Hon Lord Soames PC GCMG  
 GCVO CBE  
 Lord President of the Council  
 Privy Council Office  
 Whitehall  
 LONDON  
 SW1A 2AT

P. M. Smith

San Christopher,

MS

R  
22/10

## COMPUTERISATION OF PAYE

I have read with interest the recent correspondence on this topic, including the letter of 13 October which recorded the Prime Minister's views on the way we should proceed.

F. M. A.

2. I am sure it must be possible for officials to find a way of implementing a decision to give the contract to ICL, under our current procurement policy, without courting real risks of either international legal challenge or PAC criticism. On the international front, we should adopt a robust approach, as we agreed when we considered our general public procurement initiative in E Committee in February. The EEC and GATT codes seem to be concerned much more with tendering procedures than with the niceties of contracting and, if we have decided what we want to do, and have told Parliament and the industry, then I see little real prospect of anyone challenging us even if the formal contract is still in an early stage on 1 January. Within Europe, it is most unlikely that the EEC Commission would initiate any action against us for placing an order with ICL which those responsible for industrial matters in the Commission will almost certainly see as the best outcome for Europe. I doubt whether the foreign multinationals, who are preparing for a new relationship with UK Government purchasers as the present procurement policy is phased out, will want to seek a confrontation with us at a critical moment in that process.
3. I accept that, on the domestic front, both the evaluation of ICL's proposals and - as I hope - the subsequent action to place the contract with them will have to be undertaken with due regard to financial propriety as well as to the need for urgent action. Here again, however, I see no real practical difficulty if the will is there and if all those concerned adopt a firm and realistic approach to their task. This will be particularly

/important...





important in the final weeks of evaluation. Although I believe the multinationals will accept, in practice, our decision to give the business to ICL, I would expect them to fight hard until that decision has been announced and to use all the methods at their disposal, especially artificially low-priced alternative estimates, to undermine ICL's case for a single tender. As to ICL's own attitude, I would expect that we would want to communicate our decision to the Managing Director before making any announcement to Parliament and that he would be left in no doubt that Ministers would expect ICL to act realistically in the subsequent contractual negotiations.

4. We shall return to these questions when we meet in E Committee in a few weeks time but I wanted to set out my views now, not least because the same international and domestic considerations will presumably apply to a wider range of central Government computer procurement cases currently under consideration. It would be a serious matter if late doubts about ability to complete contract action were to rob ICL of the considerable volume of other business for which they could properly expect to qualify under the current procurement policy between now and the end of the year. I will, therefore, be asking officials to take up the progress on these other cases separately with the CTTA and the Treasury as a matter of urgency, so that we can, if necessary, review them when we meet next on the PAYE case.

5. I am sending copies of this letter to the Prime Minister, members of E Committee, the Attorney-General, the Treasury Solicitor and Sir Robert Armstrong.

*G. G. G.*

*Kear*



1. MR. LANKESTER ✓  
2. PRIME MINISTER

B/F  
ZWR

I attach a letter from four computer professionals within the Inland Revenue. The writers believe that computerisation of the Revenue is being approached from the wrong angle.

On the face of it, their approach is well worthy of study. Would you like us to ask the Treasury to comment on the questions raised, so that we can send a reply from here?

Yes

MT.

MA

20 October 1980



Alan Pol

56, The Crescent,  
Milton,  
Weston Super Mare,  
Avon

17th October, 1980

The Prime Minister,  
10, Downing Street,  
London  
SW1

R20/10

Dear Mrs. Thatcher,

A

INLAND REVENUE COMPUTER - SAVINGS

We, the undersigned, are computer professionals and are deeply disturbed by press reports that HMG intends to "computerise" the Inland Revenue at a gussed cost of £150M.

It is our contention that a course based upon large "mainframes", terminal networks and Civil Service software development is not only fit for the epithet 'old-fashioned', but worse is a recipe for a wasteful, expensive disaster, providing little if any staff saving and rendering the tax structure inflexible and error prone.

Fortunately, the requirements of the tax system both here and abroad are in essence easy to envisage (and immediately felt by many), though self-indulgently complex in part. It is this fact, that 95% of the complexity is needed for 5% of the cases, which allows you to dispense with the traditionalist proposals.

Why not let the skilled Inspectors of Taxes ferret around with the 5% difficult cases, by hand? What is then left are the 95% of easy, standard cases which can be handled by rule-governed staff. And since these cases are easy and repetitive, let computers do the bulk of the work, thus releasing many staff (half?, two-thirds?) for more rewarding work.

But what of the costs of computers and their software? Well, their task is now one of lots of simple problems instead of one enormous one - this is ideal for microcomputers, and a microcomputer each for the remaining tax clerks would be much cheaper than the giant systems proposed! The microcomputer and its file could be in local tax offices instead of bomb-proof bunkers a trunk call away, yet would offer real advantages over the present system when files need moving.

/continued



- 2 -

17th October, 1980

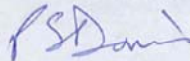
As to software, it could be so simple (for the 95% of cases to which it applied) that, provided it were not 'developed' by Civil Service staff, it could be published in the newspapers or on Prestel in the same way that computer games are. It could best be written in a computer language rightly called BASIC, which is understood by schoolchildren, and could lead to self-assessment even easier than in America.

For fiscal flexibility and for enormous cost savings now and in the future, we beg you to reject the proposals of the entrenched interests, and to open the system to truly competitive ideas.

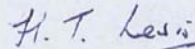
Yours faithfully,



D.L. Cutts



P.S. Davis



*H. T. Lewis*  
p.p. G. Mosley



A.H. Blake

c.c. Mr. J. Callaghan, M.P. House of Commons  
Mr. D. Steel, M.P. House of Commons



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ECON POL

10 DOWNING STREET

From the Private Secretary

13 October 1980

Dear Jim,

The Prime Minister has seen the Lord President's letter of 26 September about the computerisation of PAYE. She has also read Mr. Prior's letter of 7 October.

The Prime Minister has asked me to say that she is most concerned about the reported risk that we may not be able to meet the 1 January deadline for single tendering. She agrees with Mr. Prior that the contract must go to ICL, and that the necessary work must be completed in order to allow this to happen.

I am sending copies of this letter to the Private Secretaries to members of E, the Attorney-General, the Treasury Solicitor and to David Wright (Cabinet Office).

~ ~

Tim Laker.

Jim Buckley, Esq.,  
Lord President's Office.

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212



Civil Service Department,  
Whitehall,  
London, SW1A 2AZ

*With the Compliments*  
*of the*  
*Lord President of the Council*



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Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

The Rt Hon Sir Geoffrey Howe, QC, MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
LONDON SW1P 3AG

13 October 1980

Dear Geoffrey,

RMA

COMPUTERISATION OF PAYE

Jim Prior sent me a copy of his letter to you of 7 October.

While you will be able to assure him that no time has been lost since the E Committee meeting, and that the Inland Revenue, in consultation with the CCTA, has been pressing ahead with all speed to carry out the decision we then reached, I must make it clear that we are not yet in a position to take the decision he recommends. We must satisfy ourselves first that it is feasible and worthwhile to go ahead with a project which has been revised in the way we wanted. This involves producing a new Operational Requirement, a large task which I understand is nearing completion. It also involves examining what the revised project would cost and what benefits it would produce over what period of time, another large task on which there is still much work to do, and which depends on the adequacy of information not yet provided by ICL. In short, we must decide whether the revised project represents a good investment before we can decide on a supplier for the equipment. If all goes well, I understand that we may be in a position to reach decisions on these matters by about the end of October. But that is the very earliest feasible date.

If we then decide both that the project should go ahead and that we wish to go by single tender to ICL, we shall also have to form a view on the risks involved in trying to rush through a difficult and complicated negotiation in a very short space of time. The essence of the problem here is that once ICL know that they are to have the business, we shall be in a poor position to insist on contractual conditions which provide proper safeguards for the taxpayer and the Inland Revenue alike in what will be a very large contract indeed. I shall advise colleagues on this in due course, but I do not think the question will be an easy one.



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I have also seen the recent exchange between John Biffen and Michael Heseltine about expenditure cuts. If the project is to go ahead, it will of course be necessary to ensure that there is money in the PSA programme for its accommodation needs. It would be no good entering into any commitment to buy computers unless we know that there will be buildings to put them in.

Copies of this letter go to Jim Prior and the other recipients of his letter.

Yours ever

Christopher

SOAMES





Caxton House Tothill Street London SW1H 9NA

Telephone Direct Line 01-213 6400

GTN 213

Switchboard 01-213 3000

Rt Hon Sir Geoffrey Howe QC MP  
Chancellor of the Exchequer  
Treasury  
Great George Street  
LONDON SW1P 3AG

Prime Minister

2

To note - the  
possibility of going  
for single-tender  
seems to be  
shipping because of  
all the work that  
has to be done  
before the 1 Jan  
October 1980  
deadline. Mr Piar

*ICL has to  
submit contract  
and all  
remaining sub-  
contracts to be done.  
I'm sure I will see  
where in short it  
is.*

*cc Mr August  
Mr Wolfran*

here agree that  
we should proceed  
with ICL come what  
may. A further E  
discussion is likely  
to be necessary.

COMPUTERISATION OF PAYE

*Flas A* I have seen copies of Christopher Soames' letter to you of 26 September and the Attorney General's of 1 October.

I must say that I found Christopher's letter disquieting. Two months after we considered this question in E Committee we are told that after all we may be forced by pressure of time to put this contract out to open tender, with the strong implication that we shall then be unable to prevent its going to IBM.

I do not want to repeat here all the industrial and political arguments in favour of the single-tender system in this case: I will simply say that I agree that they are "overwhelming", as Keith Joseph put it at the meeting of E on 16 July. I respect the reservations about this course of action which were put to us then on 7 August. But in essence they are arguments against our having a public purchasing policy at all. The existence of such a policy necessarily means that we must at times like this take a longer-term view and be prepared if necessary to sacrifice a short-term advantage - although, as pointed out at our last meeting and by the CPRS in their paper (E(80)90), the IBM equipment by no means guarantees such an advantage.

I strongly believe that we should now proceed on the basis that this contract will be awarded by single tender, and that in view of all the legal and other complications to which Christopher has drawn attention we should agree to beat the 31 December deadline by concluding a contract with ICL before then. This should impose the condition on them that they must demonstrate the feasibility of their proposals by mid-1981, or whenever is judged a reasonable date. I believe this would fully respect the spirit of the conclusions we reached at E on 7 August.



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If we were to allow the contract to go to IBM we would run the risk of uniting all shades of opinion in the Commons and the country against us. I hope therefore that we can agree in correspondence to proceed on the basis I have suggested. But if not I strongly recommend that we should consider this question again at a very early meeting of E Committee.

I am sending copies of this letter to the Prime Minister, other members of E and the Attorney General, and also to the Treasury Solicitor and Sir Robert Armstrong.

*Y  
h  
J  
a*



*With the compliments of  
the Attorney-General*

*Attorney General's Chambers,  
Law Officers' Department,  
Royal Courts of Justice,  
Strand. W.C.2A 2LL*

01 405 7641 Extn. 3201





01-405 7641 Extn

*A. Inghid*  
ROYAL COURTS OF JUSTICE  
LONDON, WC2A 2LL

1st October 1980

The Rt Hon Lord Soames CH, PC, GCMG, GCVO, CBE  
Lord President of the Council  
Civil Service Department  
Whitehall  
LONDON SW1

*Dear Christopher,*  
COMPUTERIZATION OF PAYE

I have received a copy of your letter dated 26th September to Geoffrey Howe. With reference to the third paragraph I would like to point out that we have not been consulted by anyone on this matter although I understand we will be instructed by the Treasury Solicitor on behalf of the Treasury in this matter. Once we have received all the relevant papers then we will be in a position to give advice on the legal implications of the EEC rules in this matter.

I am sending copies of this letter to the Prime Minister, members of E Committee, the Treasury Solicitor and Sir Robert Armstrong.

*Yours Gov,*

*Michael Havens*



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Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

26 September 1980

The Rt Hon Sir Geoffrey Howe, QC, MP  
Chancellor of the Exchequer  
Treasury Chambers  
Parliament Street  
LONDON SW1P 3AG

Dear Chancellor,

COMPUTERISATION OF PAYE

When we last discussed the computerisation of PAYE at E Committee in early August, I doubt we were all aware of the full extent to which the new GATT and EC rules on public procurement will limit the Government's room for manoeuvre after 1 January 1981. For example, when we had a word about it after the meeting, you felt that if the reappraisal was not completed in time to let a contract before the end of the year, we could probably find some way of evading the effect of the new rules, if we decided to go to ICL by single tender. My officials have been investigating this further with the Treasury Solicitor's Department and it may be helpful if I summarise the position as I now understand it.

The new rules prescribe open tender for the procurement of computers. They provide for certain very limited exceptions, but I am advised that none of these can plausibly be used to cover the PAYE project. Single tender action with ICL after 1 January would be contrary to the new rules and risk legal action against us either by a rival manufacturer or by the Commission itself.

I am advised that once proceedings had been started, be it by another manufacturer or the Commission, the Law Officers would be likely to advise strongly against letting a contract until they were completed. Action by a rival manufacturer would break much new ground and it is difficult to forecast clearly what might happen. But in either case we should very probably lose.

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The questions which then arise are:-

- (a) If we decide to take single tender action with ICL, how far would this process have to be taken before the end of 1980 in order to avoid the risk of legal action?
- (b) Is it practicable to take it so far in the time available?

On (a), the Treasury originally took the view that it should be sufficient to issue the operational requirement and receive ICL's response before the end of the year. But your officials will now have seen the advice from the Treasury Solicitor's Department that, when the possibility of pre-emptive action in the courts is taken into account, we must reckon on being at serious risk unless we have concluded a contractual arrangement (at least a Heads of Agreement) before the new rules come into force. If moreover we wanted to ensure that the whole system was provided by ICL, the contract would have to cover the whole (albeit with break clauses), since a small initial order could not under the rules be used to justify further follow-up orders by single tender.

This has two serious consequences for (b). First, the time available for the reappraisal of the project is very short indeed. I agree that the Inland Revenue approach which you approved offers the best prospect of making an early decision possible. But there is still a formidable amount of work to complete in the time available and any slippage will make it virtually impossible to keep open the single tender option. My people will do everything possible to help, but they will need to satisfy themselves that the revised project which emerges is sound; this is essential to avoid serious problems later.

Secondly, very large risks are involved in trying to complete the contract negotiations for so large and complex a system in a few weeks against a deadline with a contractor who knows he has the business; we do not want to end up with a contract which does not control adequately what ICL is to supply, the standards it must meet, or the price to be paid. We need to look at these risks in the light, among other things, of the assurances we have given to the Public Accounts Committee about the protection of public funds in such contracts.



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We cannot, as I see it, take any decisions about this until the further work has been done and we are clear we have found the most sensible way forward. I know the Inland Revenue and the CCTA are pushing this work ahead as fast as possible and we should be able to have a further discussion of the project in E Committee towards the end of next month. But meanwhile, I want to warn colleagues that our room for manoeuvre looks like being tightly constricted, unless others see any scope for widening it.

I am sending copies of this letter to the Prime Minister, members of E Committee, the Attorney General, the Treasury Solicitor and Sir Robert Armstrong.

Yours sincerely,

*Buckley*

(Private Secretary)

for

SOAMES

CONFIDENTIAL





Treasury Chambers, Parliament Street, SW1P 3AG

B

8 August 1980

Dear Tim

COMPUTERISATION OF PAYE

I attach a copy of the Treasury Press Notice being issued today in connection with the Chancellor's announcement, together with the Notes for Editors and the briefing to be used in the Treasury Press Office.

I am copying this to Jim Buckley (CSD), Ian Ellison (Industry) and David Edmonds (Environment).

Yours

Nigel Brotherton

N V BROTHERTON  
Private Secretary

T P Lankester Esq  
No 10, Downing Street





# H. M. TREASURY

Parliament Street, London SW1P 3AG, Press Office: 01-233-3415  
Telex 262405

8.8.80

## COMPUTERISATION OF PAYE

The Chancellor of the Exchequer, the Rt Hon Sir Geoffrey Howe, QC MP, told the House of Commons today that the Government have decided to undertake further studies before proceeding with the computerisation of PAYE.

In a Written Answer to a Parliamentary Question by Mr Eric Cockeram (Cons: Ludlow), who wanted to know if the Government had yet reached a decision on the matter, the Chancellor said:

"As hon Members will know, a study of the full scale computerisation of PAYE was put in hand in 1978. These studies had reached an advanced stage when the present Government took office. The scheme produced after consultation with the computer industry involved the centralisation of computing capacity of a highly complex nature in 12 centres handling an average of more than 2 million taxpayers each.

"Despite the possible advantages of such an approach, experience shows that it carries with it a high risk of unforeseen problems, so that the expected savings and benefits are often not achieved.

"While they recognise the benefits which computerisation should bring, the Government feel that the basis on which it is to be done requires further consideration. The Government have therefore put in hand as a matter of urgency a study of alternative approaches which would diminish these risks and offer a greater opportunity of satisfactory development as the system evolves.

"The Government continues to recognise the importance of the maximum feasible involvement of UK companies and of ensuring a high UK content in the system."

PRESS OFFICE  
H M TREASURY  
PARLIAMENT STREET  
LONDON SW1P 3AG  
01 233 3415

138/80

.../.



#### NOTE FOR EDITORS

PAYE is the largest component in the Inland Revenue's workload. At present it is almost wholly manual. The exceptions are the PAYE of employees in Scotland which, since 1968, has been dealt with by a batch-processing computer system at Centre 1 at East Kilbride, involving the concentration of all PAYE staff for Scottish employees, in a single office; and an experimental 'on-line' system in six local tax offices in the West Midlands and the North West which has been running since the autumn of 1977 and in which staff deal with their daily casework through Visual Display Units (VDU's) on their desks, linked to a small central computer.

---

In 1978 the Department commissioned a study in conjunction with the Central Computer and Telecommunications Agency to test the feasibility of full-scale computerisation of all the main PAYE processes in a combined batch-processing and on-line system.

---

The proposal was to set up 12 Regional Processing Centres (RPC's) which would house a central computer system to handle the records for an average of more than 2 million tax payers each. Each Centre would also control a complex communication system linking its own operations with the other Centres as well as with individual tax offices. This network would be responsible, amongst other things, for transferring information between tax offices and regions on such matters as a change of job by the taxpayer. Staff in the 580 or so local tax offices handling PAYE would be equipped with VDU's on their desks linked directly to the Regional Processing Centres.



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Suggested defensive points for Treasury and Inland Revenue  
Press Offices

- a. General line on questions probing reasons for not proceeding with feasibility study proposals. Nothing of substance to add to the Answer. The proposals were for a project involving full scale computerisation achieved in one step throughout the country. There was the prospect of large benefits at the end of it, but inevitably, with considerable risks of technical difficulties and delay, as experience with other such projects has shown. Full benefits were not expected to accrue till the end of the decade, though the project itself was expected to be completed by 1987. Having weighed up the possible risks and benefits in light of such considerations, Ministers decided that alternative lower risk possibilities should be further explored, which involve less of a "big bang" approach.
- b. Procurement/ICL: Detailed questions on preference policy etc for Civil Service Department. But the central point is the decision not to go ahead with this particular project for the general reasons given in the Answer. These are not related to questions of procurement policy or a particular company's products.
- c. Buildings. Work in its early stages at Telford on the first Regional Processing Centre (and Development Centre for the project) - questions should be directed to the PSA.



d. Will revised project involve a commitment to ICL?  
Does the Chancellor's answer rule out a role for the US  
multinationals? Nothing to add to last sentence of Answer:  
"The Government recognise the importance of ensuring a  
high UK content in the system and the maximum feasible  
involvement of the UK companies".

e. Government has abandoned computerisation of PAYE?  
No. Remains committed to it. Decision is merely to look  
for a different way of carrying it out.

f. More detailed enquiries should be directed to Inland  
Revenue Press Office.





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DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 3301  
SWITCHBOARD 01-212 7676

PS/Secretary of State for Industry

7 August 1980

R I Tolkien Esq  
Private Secretary to the  
Chancellor of the Exchequer  
Treasury Chambers  
Parliament Street  
SW1

(12)

Dear Richard

DRAFT ANSWER BY THE CHANCELLOR ON PAYE COMPUTERISATION

Thank you for your letter of 7 August. This is to record my telephone conversation with you earlier this evening when I said that my Secretary of State is content with the draft answer proposed in your letter of 7 August subject to revision of the final sentence as follows:

The Government recognise the importance of the maximum feasible involvement of UK companies and of ensuring a high UK content in the system.

2 I am copying this letter to Jim Buckley and Tim Lankester.

Yours sincerely  
Catherine Bell  
CATHERINE BELL  
Private Secretary

PS/mung  
PS/sec  
MR Bullcock  
MR Atkinson  
MR Lingard  
(papers)

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Civil Service Department,  
Whitehall,  
London, SW1A 2AZ

*With the Compliments*  
*of the*  
*Private Secretary*  
*to the*  
*Lord President of the Council*






Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

From the Private Secretary

7 August 1980

Richard Tolkien Esq  
Private Secretary to the Chancellor of  
the Exchequer  
HM Treasury  
Parliament Street  
LONDON SW1P 3AG

*within next  
few months  
in DIP folder*



Dear Richard,

Thank you for your letter of 7 August enclosing a copy of the Chancellor's proposed statement tomorrow on PAYE. May I confirm some amendments which we would like inserted and about which Gerald Watson spoke to you earlier?

- a. Delete second sentence; this raises the embarrassing question of what Treasury Ministers have been up to for the last 15 months.
- b. Third sentence: insert "managerial" before "complexity". The scheme is not technically complex. Earlier in the same sentence "centralisation" is a hostage to fortune since it is by no means certain that a much less centralised solution will emerge from the study.
- c. Fourth sentence; delete all after "approach" and insert "it carries with it a high risk of unforeseen problems and that the expected benefits and savings will not be achieved in the planned timescale." If this is not acceptable, we must insist as a minimum on the insertion after "experience", of the words, "generally, as well as in Government".
- d. Fifth sentence; delete "would", insert "should".

I am copying this to Ian Ellison and Tim Lankester.

*Yours sincerely,  
Jim Buckley.*

J BUCKLEY





*cc Mr Harman  
Mr Wilson*

Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

*Mr [unclear]*

*Prime Minister*

*This seems about  
right*

*12  
7/8*

7th August 1980

J. Buckley, Esq.,  
Private Secretary to  
The Lord President of the Council

*D.*  
*S.M. [unclear]*  
*Adam Piskley -*  
*who with acct*  
*X; but not*

*Dear Tim,*

Following the discussion at E this morning, we have been trying our hand at an Answer to the inspired PQ in which the Chancellor is to report to the House the Government's thinking on the principle of and procurement for the computerisation of PAYE.

*XX.*

*D.*

.....

I now attach a copy of the draft Answer which I hope the Lord President and the Secretary of State for Industry will think fairly reflects the decisions taken this morning. I should be grateful if you and other recipients of this letter would indicate their Department's agreement to this draft by close of play this evening.

*8/8*

*They  
will  
also  
include  
returns  
to the  
stay  
being  
completed  
within  
a few  
months.*

I am copying this letter to Ian Ellison and, for information, to Tim Lankester.

Yours,

*Richard.*

R.I. TOLKIEN





I am not very happy about this statement. I have tried to write over

DRAFT ANSWER BY CHANCELLOR

As hon Members will know a full scale study of computerisation of PAYE was put in hand in 1978. These studies were largely completed when the present Government took office. ~~The scheme produced after extensive consultation with the computer industry involves a high degree of centralisation of computing capacity and of complexity.~~ Despite the attractions of such an approach, experience shows that too often such projects have given rise to great and unforeseen problems and the expected savings and benefits have not been achieved. While they recognise the benefits which computerisation would bring, the Government <sup>feel</sup> believe that the basis on which <sup>they would consider it</sup> this should be done requires further consideration. The Government <sup>have</sup> are therefore putting in hand immediately a study of alternative approaches which would <sup>diminish</sup> minimise <sup>the</sup> these risks <sup>and offer a greater opportunity of</sup> satisfactory development as the <sup>are</sup> system evolved. The Government recognise the importance of ensuring a high UK content in the system and of the maximum feasible involvement of UK companies.

X / ① They were based on 12 centralised, highly complex computer regional computer centres.

② A- alternative - <sup>to the present study</sup> would be a large number of computer centres - some 40 to 50 still <sup>in</sup> <sup>the</sup> many ways could prove more satisfactory. <sup>fact</sup> This means that <sup>we should</sup> <sup>have</sup> <sup>more</sup> <sup>than</sup> <sup>one</sup> <sup>distinct</sup> <sup>basis</sup>.

XX



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Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

Sir Keith Joseph  
Secretary of State for Industry  
Department of Industry  
123 Victoria Street  
London SW1

6 August 1980

*Don Kull*

As you say your letter was written in the hope of simplifying the discussion on Thursday. I think I must respond to it, however briefly, although in the ordinary way I would have felt it more appropriate to have dealt with these matters at the meeting.

As the papers by the CPRS and Christopher Soames suggest, now we have the CCTA's technical assessment we do not need further detailed probing of ICL's proposals in order to provide a better basis for a decision. That assessment shows that ICL's proposals do not meet the criteria for single tender. Hence it follows that it would not be acceptable to proceed by single tender, and we should now proceed to open tender, as I have previously proposed.

I should point out that the CCTA's assessment gives us no firm grounds for believing that ICL's standard of performance will meet the PAYE requirement in the future. I must stress this because the CPRS paper says in its annex that the Revenue accept ICL can do the job "subject to the risk of some shortcomings in performance". The Inland Revenue have never held that view, and do not now. Indeed Sir Lawrence Airey has made it clear that he would require an instruction, as Accounting Officer, to go ahead on the basis of the proposed ICL system. Nor can shortcomings in performance be lightly dismissed, since it is that problem, in the final count, which cannot be accepted in so important a project.

The reason for computerising PAYE is to have a more efficient tax system, not to provide a testing ground for industrial development. A policy of enlightened purchasing does not mean that the purpose of any contract in question should be subordinated to consideration of industrial policy. The prime consideration for all of us must be to meet the Revenue's needs,

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and, that done, to accommodate our industrial priorities to that requirement as best we can. So I cannot agree with your letter, which suggests doing the opposite.

I am sending copies of this letter to the Prime Minister, to our E Committee colleagues and to Robin Ibbs in CPRS.

A handwritten signature in black ink, appearing to read "Geoffrey Howe", written in a cursive style.

GEOFFREY HOWE

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Ref. A02830

PRIME MINISTER

Computerisation of Pay As You Earn

(E(80) 85 and 90)

BACKGROUND

The Lord President of the Council was asked at the meeting of E on 16th July to arrange for the Central Computer and Telecommunications Agency (CCTA) to prepare a further technical assessment of ICL's proposals; and to consider the possibility of commissioning an urgent independent assessment (E(80) 25th Meeting, Item 2).

2. The technical assessment is annexed to the Lord President's paper, E(80) 85. He advises against commissioning an independent assessment. This would take several months to complete. The probable outcome is that it would confirm the CCTA's view that a firm judgment on the feasibility of ICL's proposals cannot be formed until well into 1981 when they will have completed further work.

3. Subject to the outcome of further work and demonstrations by ICL over the next year, the Lord President concludes that they "can probably just about do the job". But:-

(i) The Inland Revenue would probably have considerable teething problems and might have to accept a solution which did not meet their full requirements.

(ii) ICL would probably take at least a year longer than would other manufacturers; and although the CCTA have not had the same detailed discussions with the latter, they believe that a number of them are likely to be able to meet the requirement in full with proven products.

(iii) (A new point): ICL have revised their cost estimates from £33.5 million to £42.5 million and this is likely to be at least £10 million higher than IBM and others.

4. If ICL were chosen the Lord President advises that:-

(i) There should be no commitment under the contract until they have demonstrated the feasibility of this system, in about September 1981.

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(ii) A consortium with Logica would be desirable but that would not avoid the delays or do much to reduce the problems as currently foreseen.

5. The overall project control could probably be given to a British consultancy or systems company. This would be a boost to the company concerned but would probably increase only marginally the United Kingdom content of the project. (See 9.2 of the technical assessment.) It could be a stipulation of open tender that all suppliers had to include a minimum British content; but the effect of this will be limited if the chosen manufacturer understandably wants to use proven products.

6. The CPRS's memorandum (E(80) 90) covers a useful checklist of the arguments for and against a single tender. They agree that there is no point in commissioning further detailed work, and they recommend that a decision should be reached now.

7. In his letter of 5th August to the Lord President, the Secretary of State for Industry continues to press his case for ICL. He acknowledges that there might be extra risks and costs in going for them, but he argues that these should be accepted as implicit in the Government's public purchasing policy for supporting United Kingdom firms. He accepts that any decision in favour of ICL should be conditional pending their further demonstration in the middle of 1981. He believes that ICL, together with Logica, could provide a satisfactory solution. In his paragraph 7 he questions the price differential that has now been quoted and suggests that this results from tactical moves by IBM and the other multinationals.

8. The pressure that ICL has been putting on Ministers means that their own activities have raised the stakes: it is more difficult for the Government not to award the contract to ICL, because the decision has in effect been turned into an issue of confidence. But Ministers have to weigh in the balance against that consideration not only the operational and financial risks and penalties of choosing ICL, but also the potential damage to the commercial reputation of ICL and the British software industry which would result from what would no doubt be well-publicised inadequacies of performance by an ICL system.

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HANDLING

9. After the Lord President has introduced his paper the Chancellor of the Exchequer and the Secretary of State for Industry will each want to comment.

10. In discussion you will wish to cover the following main questions:-

- (i) Should a decision be taken now or deferred either to allow for an independent assessment or for further talks with ICL? In view of the Lord President's advice the Committee may feel that an independent assessment would take too long and would serve no useful purpose.
- (ii) If a decision is to be taken now, should it be for ICL or for open tender?
- (iii) If it is for ICL, what conditions should be imposed? The main proposals are that the order should not be finally confirmed until 1981 when ICL have satisfactorily demonstrated their proposals; and that Logica should be involved. You might ask what provision would there be in the contract for cost penalties on ICL related to additional costs to the Inland Revenue attributable to the ICL part of the system.
- (iv) If the decision is for open tender, what conditions should there be? The main proposals are that the project should be managed by a British systems or consultancy company; and that, in so far as it is practicable, there should be conditions in the contract for a minimum British content.
- (v) What should be the terms and timing of the announcement? In view of the intense Press and Parliamentary interest in this the Committee will presumably wish any decision to be announced before the Recess. As the Chancellor of the Exchequer is the Minister responsible for the customer Department it is presumably for him to make it, but that is a point which the Committee will wish to decide specifically. If the decision is for open tender the announcement will have to be in terms which minimise the damage to ICL's reputation. This will require some care in drafting in order to strike the right balance between explaining why the Government has taken a decision which will be unpalatable to many and not knocking ICL too hard. 1



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CONCLUSIONS

11. In the light of the discussion you will wish to record conclusions:-

either

(i) commissioning an independent study, or other further work,

or

(ii) deciding between ICL and open tender, and noting the conditions attached to either course,

and

(iii) on who should make the announcement, when, and in what terms.

RA

ROBERT ARMSTRONG

6th August, 1980

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Qa 05101

To: MR LANKESTER

From: J R IBBS

Computerisation of PAYE

1. The CPRS has put in a short collective brief which up-dates its previous listing of the main arguments. This points out that the factors to be balanced on either side are difficult to quantify and suggests that they are unlikely to be significantly clarified within reasonable time by further investigation.
2. My view on the issue itself is that however much the limitations of ICL are re-assessed, ICL will remain clearly a second best supplier. My experience tells me that it is unwise on a complex high technology project to choose a supplier who is not among the leaders and who does not have actual experience of successfully producing and commissioning the equipment and system. It is not sensible to be the victim of a supplier's 'first time' unless there is an associated chance that if he is successful he and you will have leapt ahead of the competition. There is no potential bonus of this kind in this instance. Indeed, at best there would still be some operational penalty compared with what open tender should provide.
3. I am not even convinced that it is necessarily right for ICL to attempt this project, but I realise that many would disagree with me on this. However, if their competitors have established a wide lead with experience of projects of this kind it may be that ICL should be seeking other application sectors in the broad and rapidly growing market for computer equipment where they (either alone or with software associates) can gain a lead and hence the rewards that this can give. Even with the PAYE project ICL would not actually catch up with the competitors although the gap should be narrowed.
4. I realise that all these arguments which are summed up in a short sentence in paragraph 2 of the CPRS note have to be weighed against those relating to procurement policy and the political implications. However, I can say that the technical and commercial arguments against going to ICL look strong to me.



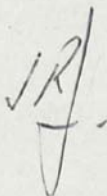
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5. It seems clear that the choice of ICL, even without subsequent unforeseen problems, would involve a substantial financial penalty due to delayed savings, a higher purchase price and some lower level of operating efficiency. The total cannot be precisely assessed but the cost of a year's delay alone has been put at £40 million. Such a sum is large in the context of steps now being taken to keep down public sector spending.

If there is in effect a willingness to envisage 'subsidising' ICL by bearing an extra cost of this magnitude, surely there must be alternative ways in which the Company could be given substantial help and without spending so much.

6. The damage done to ICL if they are not preferred would depend considerably on how the decision was presented. I would have thought that much could have been done to mitigate this if full play were made of the need to conserve public funds and to avoid delay in introducing important administrative and tax improvements, particularly if it were accompanied by positive support for ICL in some other way.

7. I am sending a copy of this minute to Sir Robert Armstrong.

A handwritten signature in dark ink, appearing to be 'J.R.' or similar, with a large flourish at the bottom.

6 August 1980



Civil Service Department,  
Whitehall,  
London, SW1A 2AZ

*With the Compliments*  
*of the*  
*Lord President of the Council*



~~CONFIDENTIAL~~  
CONFIDENTIAL



Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

6 August 1980

The Rt Hon Sir Keith Joseph, MP  
Secretary of State for Industry  
Ashdown House  
123 Victoria Street  
LONDON SW1E 6RB

Dear Keith,

COMPUTERISATION OF PAYE

Thank you for your letter of 5 August.

I still think that the computer procurement policy points clearly to competitive tender in this case. It is of course open to us to decide to set the policy aside for special reasons. But we shall only obscure the issue if we distort the meaning of the words.

I agree of course that if ICL's offering were always the best, there would have been no need for the policy. It does not have to be the best; it simply has to be satisfactory.

As regards price, my paper deliberately pitched the difference on the low side, partly to take account of the kind of point you have made. On the present figures, the ICL bid costs over 60% more than IBM's. The figures may change to some extent, but I see no way in which the difference will fall below 30% and it may be more. That is a difference we could decide to incur, but I could not call it "satisfactory".

As regards performance, the question is one of the size of the risk the Government takes at the moment it takes its decision. I do not want to make too much of this point, but the risk is there that the ICL equipment will not perform satisfactorily, and we must take it into account. We have run into serious trouble before now by hoping that ICL's product will be all right on the night. Bureau West, RAF Innsworth and the Inland Revenue Accounts Offices are notable examples.

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As regards delivery, I take the simple-minded view that "satisfactory" means that the equipment will be there and working at the time the user requires it. Hardware is useless unless the software is there to drive it properly.

Copies of this letter go to the recipients of yours.

4/  
ms en

Christy

SOAMES

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Secretary of State for Industry

CONFIDENTIAL

DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 3301  
SWITCHBOARD 01-212 7676

5 August 1980

Lord Soames PC GCMG GCVO CBE  
Lord President of the Council  
Privy Council Office  
Whitehall  
SW1

*John Christopher*

COMPUTERISATION OF PAYE

In your covering paper to the CCTA's revised technical assessment (E(80)85), you conclude that ICL's proposal does not meet any of the criteria of the procurement policy and that in principle we should therefore proceed to open tender with the contract to computerise PAYE. This is such an important conclusion that I think I should record, in advance of our meeting on Thursday, my disagreement with it, and with the way it has been reached.

2 The procurement policy which has been in force since 1971 is based on our giving contracts for computers in this power range to ICL by single tender "subject to satisfactory price, performance and delivery". There is no specific definition of what is "satisfactory", though there are clearly some commonsense rules. For instance, if ICL's offerings were always cheaper, better in performance, more proven and faster in delivery than any other company's, there would be no need for a preferential policy; some extra cost or shortfall in performance or delivery can therefore be "satisfactory". On the other hand, if ICL are manifestly unable to do a job for a reasonable price it would make no sense to entrust them with it - and, indeed, they presumably would not want to do it, since they must be supposed to have a reasonable view of their own capabilities. Between the extremes lies the area of judgement, where risks and advantages have to be balanced. That is what we will be called on to do when we meet on Thursday - and indeed, what both we and officials will have to do time and time again over the coming years if the policy of enlightened public purchasing which we agreed in E.Committee in February is to have any reality.

3 It is also important to remember that in a case of this kind the judgements are about a future standard of performance against a requirement. For instance, my understanding is that the test of satisfactory performance under the procurement policy has always been applied in terms of the performance ICL can reasonably be expected to achieve at the time the application demands it, rather

/than ...

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than what can be achieved at the point of decision.

4 My view of your conclusions - and indeed of the CCTA's assessment on which they are based - is reached against this background and in the light of the discussions between officials since we last dealt with the PAYE project at E Committee. I will deal separately with price, but I think I can summarise the points about performance and delivery which have most weighed with me, as follows:-

- a it now appears to be agreed that with one or two minor exceptions ICL will have completed all their formal development work on hardware and software for the PAYE project by the time of the demonstration.
- b CCTA have accepted that the revised demonstration proposal is sufficient to prove the company's capacity to provide a feasible system for PAYE and that it should be carried out by the middle of 1981 (i.e some six months before Inland Revenue begin their own development work).
- c The doubts that will remain after the demonstration about ICL's achievement of the full requirement and about the possibility of a year's delay in implementing the full PAYE system will stem essentially from the fact that ICL have less experience of large transaction-processing systems than some of their major competitors.
- d Those remaining doubts would be reduced if ICL's proposed association with Logica were implemented (as both companies intend).
- e Some at least of the detailed concerns about the ICL proposal (e.g the operational aspects) seem to be of the kind which user and supplier could well resolve together once a procurement decision was made.

5 Against the performance criteria of the procurement policy I think the above interpretation of the CCTA assessment could be as easily argued to point to the likelihood of a "satisfactory" outcome with ICL and Logica as to your own conclusion. As you suggest, it might be necessary to make a conditional decision, dependent on the final proof in the demonstration, but that too would seem consistent with the spirit of the procurement policy. As to the delivery criteria, I understand that its usual application is to the delivery date of equipment, about which there is no problem in this case. Interpreting it more widely (as referring also to the date of final implementation), I can understand Inland Revenue's concern at references to the risk (not the certainty, as in your conclusions) of at least a year's delay.

/Whether ...





Whether that risk might still make what the UK consortium had to offer "satisfactory" must depend on the judgement we reach on the off-setting advantages of giving them the experience other companies have already been given by pioneering customers - and we must take that judgement in the knowledge that the CSD has already pointed to the possibility of a slippage of up to two years in completion of the project, irrespective of the choice of contractor.

6 On neither of these criteria, therefore, can I agree with you that ICL fail to meet the test. Indeed, I am strengthened in that conclusion by the further information which my officials have obtained (and have passed to your officials) about the status of development work on ICL's "switch to standby" system, which affects reliability (paragraphs 5.4 and 5.7) and about the other ICL customers who will be making live use of the same set of software as Inland Revenue in the course of 1981, which affects the view of likely delays during the development of applications software (paragraph 7.3 in particular).

7 It is perhaps on the question of price, however, that I would wish to challenge most directly what you say in your paper. I recall very well that at the first of our meetings in his office on this topic, the Chancellor made it clear that he did not think the equipment price was an issue which need detain us, given the cost of the total project. Now we are told very firmly that ICL's revised proposal "is likely to cost at least 30% more" than one from IBM. The evidence for this seems to be slim in the extreme and I am not at all sure the comparison is a fair one. ICL have based their revised figure on a thorough and close knowledge of the operational requirement, using their latest and most competitively-priced computers. I gather that IBM, having apparently quoted a budgetary estimate of £39.3 million in February - very close to ICL's revised bid - put forward a far lower price within the last two or three weeks, while the public debate about our decision was at its height. But that new price (£24.8 million) assumes that only one very large computer is used at each regional centre and I understand that even the CCTA's adjustment to the comparison, referred to in paragraph 5 of your paper, would leave the majority of regional centres dependent on a single machine, in a system requiring the highest reliability. There is at least one current case in the UK private sector where IBM took business from ICL on the basis of claiming that a single large machine of this kind could do the work and where additional equipment is still being added. We should be on our guard against such claims especially when the stakes are so high for the multinationals.

8 I have set out my views at some length in this way in the hope of simplifying the discussion when we meet on Thursday. We may well find ourselves concluding that some extra risk and cost is

/unavoidable ...





unavoidable if we support the UK firms through this procurement. That should neither surprise nor frighten us, since it is implicit in the public purchasing policy we have adopted. But we should not overstate the risk or the cost and we should keep well in mind the industrial benefits and risks which I outlined when we last met and which I still consider to outweigh any disadvantages from entrusting this contract to UK industry.

9 I am sending copies of this letter to the Prime Minister, to our E Committee colleagues and to Robin Ibbs in CPRS.

*Enn en .*

*Kerr*





Secretary of State for Industry

CONFIDENTIAL

DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 3301  
SWITCHBOARD 01-212 7676

4 August 1980

The Rt Hon The Lord Soames GCMG GCVO CBE CH  
Lord President of the Council  
Civil Service Department  
Whitehall SW1A 2AZ

TL  
5/18

*Jan Christie*

Thank you for sending me a copy of your letter of 29 July to Geoffrey Howe, in which you gave your reactions to my letter of 22 July and Geoffrey Howe's letter of 25 July.

I think we are now all agreed that we should see whether we can resolve the procurement issue when we meet again in E Committee next Thursday, in the light of the CCTA's updated assessment. The work officials have undertaken together in the last day or so should certainly provide us with a fuller statement of the facts and a better focus on the key technical issues, though I agree with Geoffrey's view that we may still draw very different conclusions from that material about the level of risk implied in giving ICL the contract.

As to the possibility of an independent assessment, my objection was not to the idea as such but to the proposal that CSC could properly provide it. I think we might still want to keep the option of an independent review in mind when we meet next week, though it would clearly have implications for the timing of a final decision, as well as raising some difficult presentational problems for ICL. I was interested to note Geoffrey's reference to Pactel in this context. They are just the kind of UK consultants to whom we might turn if we chose to take such a route after all.

Finally, I really must take up your contention that when we come to consider the balance of advantage we will have firm and quantified information about the effects on the user but not about the effects on industry. In advising on ICL's ability to meet the requirement and on the likelihood of delay to Inland Revenue's timetable, CCTA officials are making a judgement about future events, some of them five years or more away, not a precise calculation from known data. But in considering the effect on ICL of denying them this contract we are dealing with the

/immediate ...

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immediate commercial realities of damage to customer confidence and the risk to specific orders in other markets at a time when, like so much of UK industry, the company is under great competitive pressure at home and abroad. I hope no-one will be seeking to understate the real industrial significance of our decision when we resume our discussion next week.

I am sending copies of this letter to the Prime Minister, Geoffrey Howe and Robin Ibbs of CERS.

*Enver,*

*Keith*



CF to note



cccsd  
constit

dsg

Econ. Pol

Correspondence in GR

10 DOWNING STREET

THE PRIME MINISTER

4 August 1980

Dear Anthony

Thank you for your letter of 23 July enclosing a letter from your constituent, Mrs. I. B. Stowas, of 19 Juxon Close, Chichester, and your reply to her, on the subject of the proposed computerisation of the PAYE system.

No firm decisions have yet been taken as to whether we should go ahead with the computerisation of PAYE. It is a very complex problem and major issues are involved. Once that matter has been resolved we shall of course consider carefully what would be the appropriate method of procurement.

Of course I understand the point Mrs. Stowas has made. The Government is fully aware of the importance of this project for the UK computer industry. There has been frequent contact throughout the planning stage between ICL and officials in the Central Computer and Telecommunications Agency and the Inland Revenue. The Chairman and Managing Director of the Company have put their views personally to the Senior Ministers involved.

The Government are giving this matter very careful consideration and will take into account all the arguments which have been put forward when the final decisions are made.

signed

Anthony Nelson, Esq., M.P.

MT

jfh





Correspondence in GR

cc: - CSD  
D/IND

10 DOWNING STREET

THE PRIME MINISTER

1 August 1980

Dear Bowen,

Thank you for your letter of 10 July enclosing ICL's submission and plea to be awarded the PAYE contract.

No firm decisions have yet been taken as to whether we should go ahead with the computerisation of PAYE. It is a very complex problem and major issues are involved. Once that matter has been resolved we shall of course consider carefully what would be the appropriate method of procurement.

I am, of course, aware of the points which Mr Murphy has made. The Government is fully aware of the importance of this project for the UK computer industry. There has been frequent contact throughout the planning stage between ICL and officials in the Central Computer and Telecommunications Agency and the Inland Revenue. The Chairman and Managing Director of the company have put their views personally to the Senior Ministers involved.

The points made then, and in ICL's submission, are being given very careful consideration. They will be taken fully into account when the final decisions on the procurement for the proposed system are made.

Yours ever

(Sgd) Margaret

Bowen Wells, Esq., MP



Civil Service Department,  
Whitehall,  
London, SW1A 2AZ

*With the Compliments*  
*of the*  
*Lord President of the Council*



Econ AD

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CCTA



Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

29 July 1980

The Rt Hon Sir Geoffrey Howe QC MP  
Chancellor of the Exchequer  
H M Treasury  
Parliament Street  
LONDON SW1P 3HE

R  
29/7

Dear Geoffrey

ICL: INDEPENDENT ASSESSMENT

Thank you for your letter of 25 July.

I don't at all like the idea of going to any outside consultant other than Computer Sciences. For they would (a) have to start from the beginning and (b) therefore need many months for the work and (c) even then it is highly questionable whether they could help us significantly more than CCTA with the core of the decision we need to take - which must at the end of the day be a matter of judgment.

So when I circulate CCTA's updated assessment to E Committee, I will recommend accordingly.

The questions we should address at E are:

- a. Whether ICL are capable of doing the job, given time;
- b. If so, how much longer than the timetable you have set are they likely to need?
- c. If the answer to (a) is an unequivocal yes, then whether we should accept this delay (which can be quantified), or risk damage to ICL (which cannot) for not getting the order.

CCTA can give their answers on (a) and (b); only we and our colleagues can decide (c). We ought to get on and resolve this before the Recess.

I am copying this letter to the Prime Minister, Keith Joseph and Robin Ibbs of CPRS.

Yours ever  
Christopher

SOAMES

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*a. M. H. ...  
M. H. ...*



*Prime Minister - Eason 18/2*

Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

*The Committee is  
prepared to accept  
further delay while  
an assessment by  
consultants is  
carried out.*

25 July 1980

The Rt. Hon. The Lord Soames, GCMG, GCVO, CBE, CH  
Lord President of the Council

*TL*

*David Christopher*

*27/7*

*mt.*

ICL : INDEPENDENT ASSESSMENT

You sent me a copy of your letter of 21 July to Keith Joseph and I have now seen Keith's reply.

I am bound to say that I can see little prospect of the CCTA's revised technical assessment securing a significantly greater measure of agreement than the original though I think it would be helpful if it set out the technical considerations in somewhat greater detail. Neither my people, nor, I think, yours, consider that ICL has provided further hard evidence since the recent round of intensive discussions to affect matters greatly.

In that event while an independent assessment of the suitability of the Company's proposed system to meet the PAYE requirement would not necessarily of itself settle the question conclusively, I agree with you that it seems to offer the best prospect of clearing the ground and achieving the maximum agreement on the purely technical issues involved before the matter goes back to colleagues. I accept reluctantly that it would involve some further delay - I think it unlikely that even if undertaken by a company like CSC with some knowledge of the project we could expect a useful report in less than say, three months - but that is an argument for putting preparations in hand right away.

I understand Keith's reservations about involving Computer Sciences, as suggested in E Committee, because of their involvement to date and their parent company's non-UK provenance. On the other hand I would have thought with you that we could rely on the objectivity of their assessment. And as you say they would be likely to provide the speediest report.

/If the





If the presentational arguments against using them are regarded as overriding one alternative would be Pactel, a UK company who have one employee - on Operational Research - in the Revenue team and therefore some knowledge of the project.

I am copying this letter to the Prime Minister, Keith Joseph and Robin Ibbs at the CPRS.

GEOFFREY HOWE

*John*



*See Mr Haslam  
Mr Haslam*

*Leon PA2*



*Prime Minister*

DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-213301  
SWITCHBOARD 01-212 7676

Secretary of State for Industry

*Sir Keith is  
unwilling to accept*

*that Computer Sciences Corp.  
would provide an independent*

22 July 1980

Lord Soames PC GCMG GCVO CBE  
Lord President of the Council  
Civil Service Department  
Whitehall  
London SW1A 2AZ

*assessment. He  
proposes that the*

*CCTA should  
up-date their  
assessment, and  
then we should*

*copies to*  
PS/Lord Trenchard  
PS/Secretary  
Mr Bullock  
Mr Atkinson  
MR Lingard (with file)

*Dear Christopher, take stock.*

Thank you for your letter of 21 July about the proposed independent assessment of the options for meeting the Inland Revenue's requirement for PAYE computerisation.

2 My understanding of the Prime Minister's suggestion at E Committee was that she felt it might be helpful to supplement the revised technical assessment by CCTA officials with a thoroughly impartial view, from a third party, on the risk of encountering serious problems or delays if we entrusted the project to ICL. She saw the possible need for this as stemming from the radically different interpretations which members of the Committee were putting on the technical advice then available to them.

2 Seen in this light, your proposal that the independent view should be commissioned from Computer Sciences Corporation (CSC) really does not seem to meet the requirement. They can hardly be described as a third party, since as you say, they have been working directly with Inland Revenue on this project for two years and it is they who played a key role in drawing up the Operational Requirement. I gather the CSC members of the Inland Revenue team also participated very actively in the series of meetings between officials and ICL late in June, on which the CCTA's original technical assessment was based. It is therefore no slur on their professional impartiality to suggest that in this case CSC could not provide us with the kind of independent view which I believe the Prime Minister felt might be of assistance to the Committee. I would also see difficulty, as you suggest, in entrusting the task to the subsidiary of a US company when the matter in question is so closely bound up with ICL's future and its competitive position against the US multinationals and when several highly reputable UK consultancy companies would be capable of giving us a truly independent opinion.





3 I think we have to be able to give ICL a reasonable assurance that they have been fairly treated in this important matter, whatever its outcome. I do not believe we could do so if we commissioned CSC to carry out the supplementary review of options.

4 I quite accept that any consultants not already intimately linked with the Inland Revenue project might well take up to three months to provide us with their view. Indeed, I imagine the same would apply to CSC if they were precluded from having any access to those consultants directly engaged in the Inland Revenue's team. I think it is still too early to conclude that a lengthier independent study of that kind will be needed. It depends on how far we are from being able to get a fair measure of agreement between officials on the facts which underpin the judgement we must make on risk. At present I am of the opinion that if my officials and the CPRS play an active part, with Inland Revenue, in helping CCTA to draw up their revised technical assessment in the next few days, then we should have a far firmer basis for our discussion when we meet again on this topic in E Committee. This seems to be what we are required to do, as a first task, in the conclusions of our last meeting. I understand that Reay Atkinson has already proposed to the CCTA the points on which their earlier assessment seems in need of expansion or updating and that he and his people are standing by to join in detailed discussions. I trust the CCTA will now be able to draw them into their work, together with CPRS and Inland Revenue officials, as a matter of great urgency, to cover also the points made by the Chancellor in his letter to me of 15 July. I believe we should then turn our minds to the possible need for a consultancy study, <sup>if necessary</sup> when we have the results of officials' further work before us.

5 I am sending copies of this letter to the Prime Minister, the Chancellor of the Exchequer and Robin Ibbes at the CPRS.

*Yours,*

*Kawz*





## LOCATION AND ACTIVITY OF COMPUTER MANUFACTURERS IN UK

### Location

The attached tables set out the location of the UK computer manufacturing and development sites ~~of ICL and of the five main~~ US multinationals (IBM, Burroughs, Univac, Honeywell and NCR), together with known details of activities, employment and date of establishment. Assisted area status is also indicated.

2 Where a plant manufactures both computer industry equipment and equipment intended for another related market (eg banking or office automation) the activity has been classified on the computer industry side. Separate plants devoted wholly or mainly to related markets (eg Burroughs' plants at Livingston and Croydon) have been identified separately. Activities in entirely different markets under different operating companies (eg Sperry activities other than Univac; Honeywell Controls) have been excluded.

3 It should be recalled that ICL was formed in 1968 by the merger of ~~ICT and English Electric Computers~~ and inherited the plants of both companies. The current pattern of ICL activities reflects the subsequent rationalisation of that inheritance. The software development centre at Dalkeith was set up following consultation with the Scottish Office in 1970 on whether a new factory or a software centre was more attractive in economic terms; the latter was preferred by the Scottish Office because it would give employment to more graduates.

4 Since ICL is the only one of these companies which manufactures its full mainline product range in this country, it is not possible to predict accurately from the attached information to what extent one of the multinationals would be able to meet the Inland Revenue PAYE requirement from UK production if the contract went to open tender and was won by one of them. This would depend on the equipment selected.

### Contribution to Balance of Trade

5 The computer industry is characterised by international production and trading. All the major US multinationals have plants in other countries, often as second sources of production for both strategic and economic reasons. In addition, there is a thriving trade in computer peripherals and terminals, some of it being intertrading within the multinationals, some the result of separate contracts on specialist suppliers. The interpretation of balance of trade figures in the computer sector is therefore particularly difficult, since a given system is frequently delivered as a series of sub-units from UK and non-UK sources for final assembly and





testing here. Until very recently it has also been extremely hard for Government to obtain firm information on the contribution of the multinationals to the balance of trade, even in confidence.

6 The overall figures show a worsening deficit in UK trade in computer equipment, from £28M in 1975 to £180M in 1979. The two main components of the deficit are thought to be the import of mini computers, peripherals and terminals (for which demand greatly outstrips UK supply at present) and the intertrading of certain of the major US multinationals whose exports from the UK lag well behind imports.

7 A separate note is attached to illustrate the known contribution of ICL and the five US companies to the UK balance of trade in computer equipment. In the case of ICL the main items imported are peripherals (which ICL do not manufacture) and certain terminals made by ICL's US factory in Utica, New York State (acquired as part of the Singer takeover in 1976). The importing of microelectronic components for the manufacture of this equipment in the UK by ICL and the other five companies is not included in these balance of trade figures; exports of microelectronic components are similarly excluded.

Department of Industry

21 July 1980



MANUFACTURING AND DEVELOPMENT PLANTS OF ICL AND US COMPUTER COMPANIES BASED IN THE UK

\* mainly in non-computer activity

LOCATION	ASSISTED AREA STATUS	DATE OF ESTABLISHMENT	NATURE OF WORK	NUMBER OF EMPLOYEES
BURROUGHS				
Cumbernauld	Special Development Area (SDA)	pre - 1960	Minicomputers and Software production. Printers.	1750
Glenrothes	SDA	1970s	Peripherals production and R & D	515
Livingston*	SDA	1970s	Bank terminals	200
Cramlington	SDA	1970s	Printed circuit boards manufacture	220
Croydon*	-	1970s	Teller terminals Cash dispensers	250
Feltham	-	Not known	Software development	880
ICL				
Dalkeith	DA (Development Area)	1970	Software development	125



LOCATION	ASSISTED AREA STATUS	DATE OF ESTABLISHMENT	NATURE OF WORK	NUMBER OF EMPLOYEES
ICL (cont.)				
West Gorton (Manchester)	Intermediate Area (IA)	pre - 1960	Development work	1500
Plymouth Grove (Manchester)	IA	1979	Pointed circuit board manufacture	500
Ashton-under-Lyne	IA	1979	Big systems manufacture	900
Winsford, Cheshire	IA <sup>98</sup>	1960s	Medium systems manufacture and development work	3360
Kidsgrove, Staffs	-	1960s	" " "	1915
Letchworth	- <sup>9</sup>	pre - 1960s	Small systems manufacture	2400
Bracknell	-	1960s	Software development	1170
Stevenage	-	pre-1960	Development work	1450
IBM				
Greenock	SDA	pre-1960	Terminals and small systems	2200
Havant, Portsmouth	-	1967	Large and medium systems	1300
Hursley Park, Winchester	-	1960s	R & D	1300
HONEYWELL				
Newhouse, Lanarkshire	SDA	pre 1960s	Large systems and minicomputer manufacture	280



LOCATION	ASSISTED AREA STATUS	DATE OF ESTABLISHMENT	NATURE OF WORK	NUMBER OF EMPLOYEES
HONEYWELL (cont)	Hemel Hempstead -	1960	Software and systems work	400
NCR	SDA	pre 1960	Manufacture of certain machines of current NCR range	1000
UNIVAC	No UK manufacturing or development plants			





CONTRIBUTION TO UK BALANCE OF TRADE IN COMPUTER EQUIPMENT

ICL

Made a net positive contribution of £53 million in 1979 (an increase on the figure of £40 million in 1978). This figure has been quoted by ICL in the context of the PAYE case.

IBM

Revealed last week to the Parliamentary Computer Forum, for the first time in public, that it made a positive contribution of £8 million last year. IBM is thought to aim for a broadly neutral contribution in all the countries - outside the US - in which it manufactures.

Burroughs

Revealed in confidence to the Department a positive contribution of £7 million last year. Has been in deficit in recent past years.

Honeywell

No figure revealed to the Department. Informal indications suggest Honeywell is currently in deficit.

NCR

No figure revealed to the Department. Believed to be currently in deficit.

Univac

Has no manufacturing plant in UK. Revealed in confidence to the Department a substantial annual deficit in computer equipment of the order of £50 million p.a. )



COVERING COMMERCIAL IN CONFIDENCE



DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB

2

TELEPHONE DIRECT LINE 01-212 3301  
SWITCHBOARD 01-212 7676

PS/Secretary of State for Industry

21 July 1980

Tim Lankester Esq  
Private Secretary to the  
Prime Minister  
10 Downing Street  
London SW1

*Ann Shute*

*Dear Tim*

*The attached table shows that Burroughs and IBM are large employers in SDA's; but about half of ICL's employees are in IA's.*

PAYE COMPUTERISATION: INDUSTRIAL ACTIVITIES

I understand that you asked, on the telephone earlier today for information on the proportion of the activities of the main computer manufacturers in the UK which is conducted in Assisted Areas, and broad analysis of the contribution made by the individual companies to the balance of trade.

... 2 I enclose the material requested; this contains the fullest information we have to hand, or have been able to obtain in the time available. I hope this meets your request.

*Yours sincerely*  
*Catherine Bell*  
CATHERINE BELL  
Private Secretary

COVERING COMMERCIAL IN CONFIDENCE





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Scan PA

Civil Service Department  
Whitehall London SW1A 2AZ  
01-273 4400

21 July 1980

The Rt Hon Sir Keith Joseph Bt, MP  
Secretary of State for Industry  
Ashdown House  
123 Victoria Street  
LONDON SW1E 6RB

*Prunthick*

*Contact provided*

*from C.S.D. 2/2/80*

*Sir Keith is ?*

*Mr. ... 21/7*

Dear Secretary of State,

I have been giving some thought to the Prime Minister's suggestion at E Committee last Wednesday that we might seek urgently an independent assessment of the options for Inland Revenue from Computer Sciences International, now Computer Sciences Corporation.

As you know CSC have been closely involved with Inland Revenue in the full study for the project and in drawing up the Operational Requirement for the last two years. Thus they have an intimate knowledge of the project unequalled outside Inland Revenue and CCTA. They have also co-operated with ICL in a number of successful (but much smaller) computer applications with characteristics similar to those of the PAYE project.

If we are to seek an independent opinion urgently it can only come from CSC; anybody else will need some months to get to grips with the requirement and the capacity of ICL sufficiently to give us an appraisal.

I can see that it can be objected that they will not come to the project afresh, and that they are the subsidiary of an American company (and they may even want to bring over a senior member of the American company to assist in the assessment); against this they will be working with Inland Revenue on the design of the PAYE system to run on the chosen computers and so share a strong vested interest in getting the answer right. We can in any case take all this into account in assessing what they say. I would have it in mind to make it plain to them that we are hiring them to give us an independent and disinterested assessment.

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My own view is that this is such a difficult decision that we would find benefit in another assessment, to set beside the updated CCTA assessment which I have set in hand. I therefore favour seeking a view from CSC about the ability of ICL to undertake the project successfully and to time. The alternatives are no independent view, or a delay in decision for up to three months.

I should be grateful to know your mind on this in the course of the day.

I am sending copies of this letter to the Prime Minister, the Chancellor of the Exchequer, and Robin Ibbes at the CPRS.

Yours sincerely,

*Quinlan*

Private Secretary.

SOAMES

(Dictated by the Lord President -  
signed on his behalf).

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Ecan P21



From the Minister

MINISTRY OF AGRICULTURE, FISHERIES AND FOOD  
WHITEHALL PLACE, LONDON SW1A 2HH

16 July 1980

PRIME MINISTER

*As I have said,*

COMPUTERISATION OF PAYE: PROCUREMENT OF EQUIPMENT

As you know, I shall not be able to attend E Committee today. Having read the three Memoranda which have been prepared on this subject, I should like to say that I attach the greatest importance to the points in paragraph 4(b) of the paper by the Secretary of State for Industry. The US multi-nationals have themselves had a long period of preference in their own country and it is only through similar treatment on our part in respect of projects of this nature that we can ever hope to see our own industry secure a sound base.

2. My own Department - and of course others - have a large investment in ICL mainframe machines and we are wholly dependent on them for much of our work. Continued support for ICL is a safeguard for this investment.

3. I also support the CPRS view that we should take all practicable steps to minimise the risks in taking single tender action with ICL.

4. I am copying this minute to members of E Committee, the head of CPRS and Sir Robert Armstrong.

*Peter Walker*

PETER WALKER

CONFIDENTIAL



CONFIDENTIAL

PRIME MINISTER

Pay as you Earn Computers  
(E(80) 68, 69 and 70)

BACKGROUND

The Inland Revenue's present largely manual PAYE system is to be replaced by a computer system by April 1987. Under the present computer procurement policy, which operates only to the end of this year, £30 million of computers and associated equipment could be procured by single tender from ICL provided that they could give satisfactory assurances on time, quality and price. The total cost of the project, including terminals and software and buildings, is in the order of £150 million.

2. In their memorandum E(80) 68, the Chancellor of the Exchequer and the Lord President of the Council say that they are not persuaded that ICL can give the assurances necessary to justify single tender. Their judgment is based on technical advice from the Inland Revenue, assisted by consultants, and the Civil Service Department's Central Computer and Telecommunications Agency (CCTA). They argue that ICL, in contrast to the multi-nationals, are offering an unproven system. This could well lead to delays, at a cost of £40 million a year mainly because of deferred staff savings. Major changes in tax policy could be held up; and 1 million employers and 27 million employees affected if there were major problems with the new system. They reluctantly recommend open tender and point out that some of the multi-nationals have substantial manufacturing capacity in the United Kingdom.

3. In E(80) 69, the Secretary of State for Industry argues forcefully for going to ICL by single tender; and he attaches the letter of 4th July to you from the Chairman of ICL. The Secretary of State is persuaded that ICL could deal with the risks. He points out that if they were not to get this contract there would be considerable damage to their international standing and their future prospects from, effectively, a vote of no confidence in them by Her Majesty's Government. He further points out that an adverse decision could call in question the credibility of the Government's new public purchasing policy.

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4. The CPRS' paper, E(80) 70, offers a summary of the arguments on either side, with a useful tabulation in the Annex. They suggest some further points which might be pursued before a final decision is taken, namely:-

- (i) if single tender were approved, ICL should be required to work closely with one of the leading United Kingdom software and system companies (such as Logica) with a view to getting the best results both for the Revenue and the United Kingdom information technology industry (their paragraph 8(a));
- (ii) if the decision were for open tender, the industrial damage might be mitigated if arrangements were made for United Kingdom software and systems companies to participate in the design and development work, or even in the management of the project (paragraph 8(b));
- (iii) either way, the terms of the tender should ensure that the lead company could not limit the opportunity for United Kingdom suppliers to compete effectively for the subsequent contracts for terminals, and network, hardware and software.

HANDLING

5. The Chancellor of the Exchequer and the Lord President, the Secretary of State for Industry and Mr. Ibbs will each wish to speak to their papers. Other Ministers will then wish to comment on the alternatives and to put questions.

6. I understand that you will not wish to reach a final decision at this meeting. The discussion might therefore centre on commissioning the further work which may be necessary before a final decision can be taken. I suggest that, in view of the considerable Parliamentary and Press interest generated by this project and of the need to make progress with the contract, you might aim to take decisions in time for a statement before the Recess. This points to further discussion by E in the week beginning 28th July. The further points which Ministers might wish to explore are:-



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(i) What are the employment consequences of the alternatives?

I understand that the direct employment consequences are relatively insignificant since the computer orders would be spread over a number of years. However, the Secretary of State for Industry can advise colleagues on this; and he will no doubt want to stress that it is the indirect and longer term consequences of losing this order which matter for ICL. Even so, if the decision were for open tender, the Committee may well wish to insist that the company concerned should manufacture as much as possible in the United Kingdom.

(ii) What further conditions should there be if there is to be single tender to ICL?

Here Ministers will wish to consider the CPRS' proposal, in paragraph 8(a) of their paper, that one of the leading United Kingdom software and system companies should be involved. You might also question to what extent the contract would provide for penalties on ICL if they were to be responsible for delays.

(iii) What should be the conditions if Ministers were to favour open tender?

The Committee will wish to consider the points in paragraphs 8(b) and 9 of the CPRS paper on the participation of United Kingdom software and systems companies and on the scope for ensuring that the successful company (whether ICL or a multi-national) would give opportunities for United Kingdom suppliers to compete effectively for subsequent contracts for ancillary equipment.

CONCLUSIONS

7. On the assumption that the Committee will not reach a final decision, you will wish to invite the Lord President of the Council to arrange for officials of the Central Computer and Telecommunications Agency, in consultation with the Department of Industry, the Inland Revenue and the CPRS, to report further on:-



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- (i) the proposals in paragraphs 8(a) and (b) and 9 of the CPRS paper (E(80) 70);
- (ii) any further questions raised in discussion; and in time for discussion by E in the week beginning 28th July with a view to a statement before the Recess.

RA

(Robert Armstrong)

15th July 1980

CONFIDENTIAL



15 July 1980

Policy Unit

PRIME MINISTER

cc Mr Wolfson

INLAND REVENUE COMPUTER

1. We think you should try to establish at an early stage whether the committee agrees that on industrial policy grounds - and political grounds - we would prefer the contract to go to ICL and the British software industry, if the risks and costs are not too great. To put it another way, are we - as Keith has often said we are - attempting to operate a public purchasing policy?
2. If there is no general view that it would be preferable to buy British unless the penalties are really serious, then there is not much more to discuss except the presentation of a decision to go to open tender.
3. But if the committee agrees that in principle some penalty can be accepted as the price of helping the British industry to acquire new experience, attention should focus on the size of the technological gap that ICL has to jump, the risk that it will fail, and the cost penalties. These cannot be thrashed out in E Committee on the basis of evidence available.
4. The CCTA assessment is that ICL can probably do the job. Logica's involvement in the consortium makes this more likely and spreads the national benefits more widely. So things have improved since the CCTA assessment was made. They thought the penalty was twofold:
  - (1) a risk of a delay of one year;
  - (2) a comparatively "inelegant" system.
5. We think these two penalties ought to be more precisely analysed before a decision is made. If this was done by an independent third party, it would help the Government to sell the final decision, whichever way it went. At present, we do not know how likely the one-year delay is, nor how serious or unavoidable the "inelegance" is.
6. David has suggested the third party idea to Mr Watson of the CCTA. He saw its merits and thought that Computer Sciences International might be well-placed to undertake the evaluation. It should be possible in my view to do this in a few weeks.




7. Suggested Agenda

In summary, the meeting should answer the following questions:

- (1) Do we in principle want ICL/Logica to get the contract, though not at any price?
- (2) Do we agree on the need to know the size of the gap ICL/Logica has to jump, the risk that they won't make it, and the cost of the consequences?
- (3) Should we obtain a third party view (eg from Computer Sciences International or similar) to analyse the gap/risk/penalty as a basis for decision and presentation?

I have copied this minute to Robert Armstrong and Robin Ibbs.



JOHN HOSKYNS





Ph mt in  
E H  
(Ph H)

Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

15 July 1980

11/7

The Rt. Hon. Sir Keith Joseph, MP  
Secretary of State for Industry

*In kin*

ICL AND PAYE COMPUTERISATION

Thank you for your letter of 11 July in which you say that no-one is suggesting that ICL will be unable to provide an "adequate" system to support PAYE, given time.

I do not think that that reflects my view based on the CCTA's technical assessment. The issue is not simply one of giving ICL more time. We need to be as sure as we reasonably can not only that we minimise the technical risks during implementation but that we get a system which works satisfactorily, not just adequately, once PAYE is computerised. That is surely what the current preference policy in favour of ICL requires when it specifies satisfactory price, performance and delivery.

Paul Channon may wish to comment, but the CCTA technical assessment, as I understand it, is that not only will there be delay to the project before ICL can put together the full equipment and software to let the Revenue carry out the detailed design and development of the new system, but even then the solution proposed is likely to be operationally unattractive. There is the real risk that such a system would be liable to breakdown requiring intervention by computer operators to keep it going or to delay in responses at the local office level. Frankly I would not regard such a system as "adequate" for an operation of the magnitude and importance of PAYE.

I am copying this to the Prime Minister and to Paul Channon.

*y*  
*Howe*

GEOFFREY HOWE





Civil Service Department

*John Ashby*

→ *E Barker*

Central Computer and Telecommunications Agency  
Riverwalk House, 157/161 Millbank, London SW1P 4RT

from the Director

Telephone: 01-211 7704

*15th July 1980*

*Jana Hoffman, G  
Co, Sunny Hill  
Surrey*

*PACU*

*Dear Jana,*

*Enclosed in*

*technical report which we*

*spoke about a few minutes ago.*

*I hope it is helpful.*

*Yours sincerely  
David [Signature]*



TECHNICAL ASSESSMENT OF ICL PROPOSAL TO SATISFY INLAND REVENUE  
(PAYE) REQUIREMENT  
(Note by Head of Technical Services, CCTA)

1 There are two main questions:

a will the ICL proposal satisfy the Operational Requirement in respect of performance, availability, operation and timescale?

b are the company capable of demonstrating their proposal successfully in their stated timescale (ie by end of March 1981)?

2 CCTA have now completed, during the last week, three days of intensive discussions with ICL about their proposals; officials from DI and Inland Revenue were also present. Nevertheless there are no clear black and white answers to either of the questions or to any of their component parts but the following paragraphs deal briefly with each.

3 Proposal

3.1 Performance

In principle the company have prepared an outline design which appears to be the basis for a viable solution; but there is a potential shortfall in performance. The company have admitted that they had (due to a misunderstanding) assessed the workload based on one hour of peak activity instead of 4 hours; moreover, during this peak period there is only a 10% contingency. They also acknowledge that the sizing did not include a number of factors (eg batch, operations and network control overheads and realistic inter- and intra- regional traffic). At best the performance is likely to prove marginal in the larger regions to meet the peak conditions as defined. In principle the shortfall could be overcome by the addition of further equipment but this can only be confirmed by completion of a detailed sizing which is likely to take up to 3 months.

3.2 Availability/reliability

ICL have quoted reliability figures for the S3 system on which their proposal is based significantly above those previously notified by the company to CCTA. Those already known to CCTA are consistent with those being achieved by the smaller S range systems, and it would be unwise to assume figures better than these. Because of the nature of the ICL proposal, the Inland Revenue Requirement in this area will have to be restated and it is currently unclear whether the ICL proposal will meet it; the Revenue may need to review the acceptable level of interruption of service to local offices. An additional unknown factor relates to the effectiveness of the automatic detection and "switch to standby" system which has yet to receive detailed consideration by the company.



### 3.3 Operation

The detailed operational aspects of the proposal have not yet been considered by either ICL or Inland Revenue. The solution, as proposed, is not attractive and its manpower and performance overheads have yet to be assessed. Inland Revenue have referred to these as likely to be 'horrific' which contrasts with ICL's apparent lack of concern; the truth will probably be between the two, but the operational implications of an inelegant design cannot be ignored.

### 3.4 Timescale

The ICL proposal requires the use of much equipment and software which has not been used previously in operational circumstances and much which is still in development. There are also aspects of the outline design, which, when examined more closely, are almost inevitably going to reveal further problems. ICL have little previous experience with communication based computer systems of this scale and it is common knowledge that all other companies have had to overcome significant difficulties in their first development and application for this environment it is no criticism of ICL to expect that they will also meet problems.

### 3.5 Conclusion

There is no reason in principle why the ICL proposal could not form the basis of a successful solution to the Inland Revenue Requirement; it is, however, cumbersome compared with the solutions which some other companies might propose. This lack of elegance is the consequence of limitations in their available product range and architectural design concepts. There is a significant possibility that the amount of equipment may have to be increased to satisfy the performance (and perhaps availability) requirements unless the Revenue requirement can be made less exacting; this will increase the complexity and cost. Since the proposal is also based upon much new equipment, and software not yet used operationally; since the design has not yet been developed in detail; and since ICL have not yet much experience in the development and setting to work of large communication based systems: the risk of slippage to the Revenue timescale is probably in excess of a year.

## 4 Demonstration

### 4.1 Adequacy

ICL have proposed a partial demonstration, composed of one sub-region module with the standby module, which is intended to represent the full workload of each module plus the interconnection arrangements; they consider it unnecessary to build a whole region to demonstrate their capacity to meet the whole Requirement. However, they have now agreed to provide simulation of the load of the other sub-region modules; but this may put at risk their end of March date for demonstration. ICL will not have sufficient equipment available in the timescale to mount a larger demonstration.

We believe the ICL demonstration proposals, enhanced to provide simulation of missing sub-regions, would be sufficient to prove ICL's



capacity to carry through the Revenue Requirement, provided the total loads are assessed carefully, since there is likely to be a performance shortfall. The company will also need to satisfy us that, should there prove to be a performance shortfall, additional equipment can be connected in an operationally viable manner to overcome this.

#### 4.2 Timing

There is undoubtedly confidence in the company in their capacity to mount a demonstration successfully by end of March 1981, but they recognise that availability of equipment (particularly S3 machines) puts a tight constraint on the timescale. CCTA also believe that the enhancement to the work (ADNET) currently being performed under a DI development contract may prove greater than ICL admit; but against this it has to be recognised that the ADNET team are very familiar with their tool.

There must therefore be significant risk to a demonstration date of end of March 1981 for logistic and development reasons (plus the potential impact of industrial action within ICL); but we would have reasonable confidence that the delay should not exceed 2-3 months. But if the demonstration is based on ICL's present sizing there is a significant risk of it failing to provide adequate performance (see 3.1 above). This may not be serious provided that the company can satisfy us that the configuration can be viably extended.

#### 5 Summary

From the evidence available we conclude that there is a prima facie case that ICL could provide, given time, a technically acceptable solution to the Inland Revenue Requirement; however, there must be significant risk to the proposed timescale of the project of at least one year brought about by the use of much new equipment and software, by system design problems yet to be properly appreciated, and by the company's inexperience of such systems.

We also conclude that ICL would find it difficult to run an acceptable demonstration by March 1981, but that slippage should not exceed 3 months. However, the demonstration would, on present evidence, be likely to show a performance shortfall; this could probably be remedied (at extra cost and complexity).

While, if delays are acceptable to the Inland Revenue, we would have reasonable confidence that the ICL proposals represent a viable method of meeting the Requirement in time and that this can be acceptably demonstrated by mid-1981, they do not represent an attractive solution to the Requirement, largely due to the intrinsic inelegance of the design. More attractive solutions would undoubtedly be proposed by other companies.

*RA*  
R A BALLARD  
1 July 1980



①

ADDENDUM TO TECHNICAL ASSESSMENT OF ICL PROPOSAL TO SATISFY  
INLAND REVENUE (PAYE) REQUIREMENT.

(Note by Head of Technical Services, CCTA).

Since writing the Technical Assessment at 1 July 1980, there have been further discussions with ICL to pursue some of the aspects of concern. In particular, these have concerned other Company projects for Transaction Processing Systems, Reliability and Automatic "Switch-over to Standby" techniques.

We are now aware of a development for a similar application at Barclay's Bank in South Africa; however, since the scale of the project is very much less, its timescale similar to PAYE but using different system software this experience is unlikely to influence greatly ICL's competence to satisfy the Revenue requirement timeously. Work has now been committed to enhance the resilience of the software to improve the reliability of the system; this work will not complete for some two years but one can have reasonable confidence that its targets will be achieved. This reliability improvement is likely to be insufficient to make unnecessary the Standby feature of the ICL proposal and it is evident that effective automatic switchover methods have not yet received detailed consideration by the Company and their practical effectiveness remains in doubt.

These discussions have re-affirmed the view therefore that while ICL should be able to meet the Inland Revenue requirement given time, there is significant risk that the proposed Project timetable is likely to slip by at least one year.

10 July 1980





Logica Holdings Limited

64 Newman Street  
London W1A 4SE  
England

Data processing  
Communications software  
Data communications  
Systems engineering  
Management sciences  
Mathematical analysis

PABH/HMB/H456

14 July 1980

telephone 01-637 9111  
telex 27200

The Rt. Hon. Mrs. Margaret Thatcher, MP  
10 Downing Street,  
London. SW1.

**Logica**

*Dear Prime Minister,*

THE PROPOSED AUTOMATION OF PAYE FOR THE INLAND REVENUE

I understand that this week you and your colleagues are to discuss the supply of equipment and associated software for the proposed automation of PAYE. If the Government decide to go single tender to ICL, then ICL and Logica will form a consortium to bid for and undertake this project.

The formation of the consortium is for the moment precluded by the Civil Service Department whilst the procurement procedure is being decided upon. This is because of my own personal association with the project during the past two years, first as a member of the Chairman's Steering Committee and second, as a member of the Review Team called for by the Chancellor of the Exchequer.

I write to say that I am confident that together ICL and Logica can meet the needs of the Inland Revenue on this project. I say this fully aware of the task to be undertaken, the capabilities and resources that are needed, and the risks involved. Furthermore the successful joining together of ICL and Logica in this consortium would set a precedent with major potential export benefits for the UK computer industry in the fiercely competitive international market place.

*Yours sincerely,*

*Philip Hughes*

Philip Hughes  
Chairman

directors  
C J F Botcher  
P J Coon  
P C Harbridge

P A B Hughes  
H N P McCorkell  
D W Mann  
L A Taylor

registered office  
64 Newman Street  
London W1A 4SE  
England

place of registration  
England  
registered no  
1389044





DG

c. ANT

10 DOWNING STREET

*From the Private Secretary*

11 July, 1980.

Dear Mr Chappell,

The Prime Minister has asked me to thank you for your letter of 4 July about the procurement of computers for the Inland Revenue's proposed PAYE project. She notes that you have put your views personally to the senior Ministers involved in this question. The points you made then, and in your letter, are being given very careful consideration, and the Prime Minister does not feel that a further personal meeting at this stage would be likely to add to the very full understanding the Government now has of the Company's position with regard to this particular project.

Yours truly,

Tim Lasker

E.P. Chappell, Esq., C.B.E.

Sup





*Geoffrey Howe*

DEPARTMENT OF INDUSTRY  
ASHDOWN HOUSE  
123 VICTORIA STREET  
LONDON SW1E 6RB  
TELEPHONE DIRECT LINE 01-212 3301  
SWITCHBOARD 01-212 7676

Secretary of State for Industry

11 July 1980

Rt Hon Sir Geoffrey Howe QC MP  
Chancellor of the Exchequer  
HM Treasury  
Treasury Chambers SW1

*John Geoffrey,*

ICL AND PAYE COMPUTERISATION

1 I should like to enter this postscript to last Thursday's meeting.

2 No-one is suggesting that ICL will be unable to provide an adequate system to support PAYE. The concern is over delay. But whether, and if so to what extent, selection of ICL as opposed to another manufacturer will increase the risk of delay is a matter of conjecture, not certainty. In this connection I understand that the CCTA have pointed out that the main risk of delay to the overall programme (which is not scheduled for completion until 1987 at the earliest) will lie in the work for which the Inland Revenue is responsible - and not to possible delay attributable to ICL in the very early stages of the project.

3 What is certainty, not conjecture, is that the loss of this major contract (coming so soon after the decision on the CAA radar) will strike a further extremely damaging blow at the UK's electronics industry which hitherto has been one of our success stories. This is not simply a question of jobs or loss of morale among the skilled workforce of ICL - or even of a reduction in immediate earnings. It puts at serious risk what is generally acknowledged (even within the industry itself) to be the key component in the UK's indigenous computer industry; ICL has production plants and software design facilities ranking with any in the world in terms of equipment, skills and quality of product.

4 I recognise of course that the Inland Revenue have not had an altogether happy experience with ICL in the past and that they have an understandable concern to reduce, as far as possible the risks and problems which are inherent in any major computer project. However the fact remains that ICL's new products have

PS/LORD Trinchard  
PS/MR Mitchell  
B/sec  
MR Bullock  
MR Lingard  
MR Austerberry  
MR Atkinson (on file)

/stabilised ...





stabilised significantly, and its general performance significantly improved, over recent months. This process will continue throughout the quite considerable period which remains before the first equipment is required next year. In this situation I am convinced that a decision not to award the contract to ICL will generate vociferous criticism of a kind which we will not effectively be able to rebut by pointing to possible difficulties at a future date.

5 My conclusion is this: the choice is between a possible marginal additional risk if we select ICL for this project, and the certainty of severe damage to ICL if we try to protect ourselves from this potential risk.

6 I am copying this letter to the Prime Minister and to Paul Channon.

*Erin even i*

*Kerr*





*T. J. J.*  
*Carret?*  
*MAJ*

Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000

10 July 1980

M Pattison Esq  
Private Secretary  
10 Downing Street

*ppsect.*

*Dear Mike,*

You wrote to me on 7 July enclosing a copy of a letter of 4 July to the Prime Minister from Mr Chappell, Chairman of ICL, about procurement of the computers for the Inland Revenue's proposed PAYE project.

The Chancellor discussed this briefly with the Prime Minister when he saw her this morning and it was agreed that she would not take up the Company's request to see her personally, at least at this stage.

... I suggest the attached reply.

*Yours sincerely,*

*Richard Tolkien*

R I TOLKIEN



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R.  
A  
DRAFT LETTER FROM THE PRIME MINISTER TO  
E P CHAPPELL ESQ CBE, CHAIRMAN ICL

~~You wrote to the Prime Minister on 4 July~~  
about the procurement of computers for the  
Inland Revenue's proposed PAYE project.

The Prime Minister has asked me to thank  
you for your letter. She notes that you  
have put your views personally to the  
senior Ministers involved in this question.  
The points you made then, and in your letter,  
are being given very careful consideration  
and the Prime Minister does not feel that  
a further personal meeting at this stage  
would be likely to add to the very full  
understanding the Government now has of the  
Company's position with regard to this  
particular project.





ICL Ltd

10 DOWNING STREET

*From the Private Secretary*

7 July 1980

I enclose a copy of a letter from ICL to the Prime Minister about the Inland Revenue PAYE computer project.

ICL's Chairman sets out the company's view of the case for single tender procedure, and asks for a meeting with the Prime Minister to press their case.

I should be grateful for your advice as to how the Prime Minister might respond. It would be most helpful if this could reach us by Friday, 11 July.

I am sending copies of this letter, and its enclosure, to Catherine Bell (Department of Industry) and to Jim Buckley (Lord President's Office).

MAP

Richard Tolkien, Esq.,  
HM Treasury.

off





10 DOWNING STREET

*From the Private Secretary*

7 July 1980

I am writing on behalf of the Prime Minister to acknowledge your letter of 4 July about the Inland Revenue PAYE computer project.

This is receiving attention and a reply will be sent to you as soon as possible.

E.P. Chappell, Esq., CBE.

MAP

OSG





The Rt. Hon. Margaret Thatcher MP.,  
Prime Minister,  
10, Downing Street,  
London, SW1.

4th July 1980

Dear Prime Minister

The forthcoming Inland Revenue PAYE Computer Project is a procurement of critical importance to both ICL and the British computer industry.

The current procurement policy is designed to help strengthen the British computer industry to compete effectively against the dominant U.S. suppliers, who already hold a 70% share of the world market, and 85% of the EEC market.

A successful partnership exists between ICL and Her Majesty's Government. It has been reflected in the availability of development support through the mid 1970's, and the procurement policy for this high technological industry. It demonstrates that backing commercial winners by enlightened procurement does work. ICL's management over the years has responded to this opportunity and the U.K. now has a significant presence in the world computer industry. This national asset compares favourably with the German and French industries which with much greater support have done less well.

We have now had the opportunity of meeting your Ministers who are currently deciding whether to proceed to single tender with ICL for the PAYE Project, or to authorise open tendering when bids would also be invited from U.S. suppliers. If this happens it will, in our view, be seen as a public expression of Her Majesty's Government's lack of confidence in the national computer industry.

There can be no call for such a lack of confidence. I can assure you that ICL has the human skills and the technology to carry out the job successfully. ICL's management is totally committed to that success.

The PAYE Project is attracting widespread attention and comment in Parliament, the computer industry, and the international press. Speculation that the order may go to open tender and not to ICL under the terms of the present Government procurement policy is also arousing concern in the City.

ICL's 1979 positive contribution to the balance of payments of £53 millions helped to contain the current annual deficit of nearly £200M created by those U.S. suppliers who might expect to bid against ICL for this Project.

E P Chappell CBE  
Chairman



Should the PAYE order go to open tender, then irrespective of the outcome, ICL's competitive position at home and especially overseas would undoubtedly be damaged as well as that of the other British software and communication equipment companies who would be working on the project with us. The wider strategic implications of this order go beyond just the interests of ICL.

On the other hand, the award of this highly important order to ICL will be seen everywhere as a signal mark of your Administration's confidence in British industry, and in my Company.

I believe ICL deserves and has earned the full support of Her Majesty's Government as a British company which by any standard is demonstrating success and Britain's will to win, despite severe competition and present economic uncertainties. Your approval for Her Majesty's Government to proceed to single tender with ICL under the terms of the current U.K. procurement policy is therefore strongly urged.

ICL can meet the requirements of Inland Revenue, and the charge to do so will be undertaken with dedication and the full resources of my Company.

This is such an important national issue that I would request the opportunity of visiting you with Dr. C.M. Wilson, our Group Managing Director, to secure your support.

Yours sincerely,

*Philip Chappell*

E.P. Chappell  
Chairman





Prime Minister 2

To glance.  
economic policy.  
R  
7/12

Treasury Chambers, Parliament Street, SW1P 3AG  
01-233 3000

7th December, 1979

Dear Tim,

I understand that the Prime Minister,  
like the Chancellor, expressed some interest  
in the Sunday Times piece on computerisation  
of PAYE. I attach a copy of a note  
by Sir William Pile on the article, together  
with a copy of the article itself.

I am copying this letter to  
Sir William Pile's Private Secretary.

Yours,

R. I. TOLKIEN

T. P. Lankester, Esq.,





THE BOARD ROOM  
INLAND REVENUE  
SOMERSET HOUSE

4 December 1979

✓  
Lug 7

CHANCELLOR OF THE EXCHEQUER

PUBLIC ACCOUNTS COMMITTEE : COMPUTERISATION OF PAYE

...  
1. You may have seen the brief report in this week's Sunday Times on what I said to the PAC on 19 November about our PAYE computer project (copy attached). As the report quotes some of my remarks rather out of context, I thought you might welcome a brief comment from me.

2. The PAC questioned me about the study which we published last March (PAYE - Possible Future Developments) examining the implications of computerisation for possible future changes in tax policy. The answers I gave summarised the results of our study; there was nothing new in what I said.

3. On short-term benefits, I made the comment that it was still possible to introduce the taxation of benefits manually before the computerisation project got fully under way. As you know, we have been working towards introducing taxation

cc Chief Secretary  
Financial Secretary  
Minister of State (Lords)  
Minister of State (Commons)  
Sir Douglas Wass  
Sir Lawrence Airey  
Mr Littler  
Mr Lovell  
Mr Corlett  
Mr Cropper  
Mr Mower

Sir William Pile  
Mr Green  
Mr Boyd  
Mr Gracey (origin)  
Mr Painter  
Mr Houghton  
Mr Rogers  
Mr J P O Lewis  
Mr Matheson  
Mr Stewart



of unemployment benefit by April 1982; this is a feasible - though tight - timetable, but clearly there is little we can say publicly about it at this stage.

4. I did say that we could not implement tax credits or self-assessment until the system has been computerised. This is not a case of computerisation preventing changes which would otherwise be possible, as the Sunday Times implies; we explained in our published study why neither of these changes could be introduced satisfactorily without computers, and the most practical road towards them - indeed, almost certainly, the only road - is to start by computerising the present system.

5. Our study quoted expenditure tax, local income tax and greater graduation of income tax as reforms which would be helped along by computerisation but would still not fit easily within the present PAYE system. For an expenditure tax, we would have to look not only at the taxpayer's income but also at his other receipts and his savings; for a local income tax, we might have a multiplicity of local rates; and for a very highly-graduated income tax, with no basic rate, deduction of tax at source from many types of income would be much less likely to produce the right answer automatically. So for all these changes, we should probably have to make many more end-of-year assessments than we do now; and the precise coding and cumulative deduction provided by the present PAYE system would serve little purpose because an assessment would often be needed at the end of the year anyway. The computer system devised for PAYE (and possibly the underlying departmental structure) could not, as they will stand, cope with these; they would need to be adapted, probably fairly radically. Selective quotation of my explanation of this to the PAC



makes it sound as if we are ruling out these options for all time, but I think that the transcript, when it is available, will make the position clear.

6. The Sunday Times article also suggests that from 1983 to 1987 "any alteration to the tax system" will be virtually impossible. In my evidence to the PAC, I made the point - which will, of course, be familiar to you - that from 1983 to 1986, when our computer system is actually being introduced by stages, it will not be possible to make structural changes in the tax system. But I made a point of saying to the PAC that we expected to be able to cope with normal Budgetary changes throughout that period.

✓  
✓  
7. I have considered a letter to the Sunday Times spelling matters out, but on the whole I doubt if this would be worth while. I thought, however, that I ought to let you have a note, in case the Press reports led you to think that we had altered our position. I believe that No.10 have also shown an interest in the Sunday Times report, and you may like to send them a copy of this note.

William Pile

William Pile



DECEMBER 2 1979

# NEWS



## Computer puts bug in Tory plans to reshape tax system

by Patience Wheatcroft

GOVERNMENT plans to tax short-term benefits to strikers' families may be delayed until 1987 unless decisions are taken rapidly. Sir William Fife, head of the Inland Revenue, has warned MPs that any drastic changes involving the structure of the tax system, such as a switch to self-assessment or tax credits, are virtually ruled out before 1987. In effect, any such reforms must be decided within the next three months.

Mrs Thatcher's wish to tax strike pay and supplementary benefits, which she believes prolong strikes, could be thwarted for the life of this Parliament unless the Revenue is given firm instructions soon. "Time is running out, and the window is closing," declares Sir William.

At the root of the problem is the invention which was supposed to open doors rather than close windows, the computer. The Revenue has just completed a 22-month feasibility study for computerising the tax system. Once it gets the government go-ahead for the computerisation, expected early next year, any alteration to the tax system will be extremely costly and unwelcome, and, from 1983 to 1987, virtually impossible.

MPs heard of how their hands would be tied on future taxation policy when Sir William appeared before the Public Accounts Committee.

Asked what policy changes might be implemented before 1987, he replied: "Well, at a push it is still possible to alter the taxation of short-term bene-

fits manually. There is still a window that is available to do that... if the Government... knew what they wanted to do and acted quickly."

Sir William made it clear, however, that self-assessment or tax credits would be impossible to implement before the computer system is fully operational in 1987. Other alternatives to our pay-as-you earn system are being excluded because of the computer system likely to be adopted.

"I am fairly sure we could not switch to an expenditure tax and use that same system," said Sir William. "We could not, I think, live with the introduction of a local income tax... And I don't think we could switch to a very highly graduated income tax."

At current prices the computer system is likely to cost around £130m. If Ministers give the expected green light, the contracts for hardware should go out for tender early next year and be awarded by early 1981. Computerisation will be phased in between 1983 and 1986.

The Revenue argues that once the system is fully computerised, it will be far more flexible. It insists that without the computer any switch to tax credits or self-assessment would be quite out of the question. But for any Chancellor of the Exchequer to be so limited in taxation policy for such a prolonged period must be unprecedented.

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