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# Counter Measures

## A new vision for local postal services



INVESTOR IN PEOPLE



Essex County Council

The Policy Team at Essex County Council exists to analyse and advise, helping key decision makers in Essex and beyond understand the challenges that face our organisation and our communities and to evaluate possible solutions.

We bring an outward-looking, realistic perspective to our work – one that is well informed by analysis and research.

### **About the Authors**

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**Essex County Council’s vision is to deliver the best quality of life in Britain, providing excellent services and securing the future of our county.**

We call this vision **EssexWorks**, in acknowledgement of the work ethic, entrepreneurialism and pragmatism of the people of Essex, and in recognition of the fact that our residents enjoy living here and are proud of the county.

## Foreword by Lord Hanningfield

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Over the past few years, Essex, like other areas, has lost many of its post office branches. Around 300,000 people have had a branch close within a mile of their home.

These closures have been damaging. At the local level, the post office is as much a community asset as it is a commercial operation. Earlier this year, I spoke in the House of Lords about the role post offices play in keeping older people active and involved in their community. And local branches do much more besides – they support local trade, provide a trusted access point for public information and, in many rural communities, are the only route through which many residents can access banking and financial services.

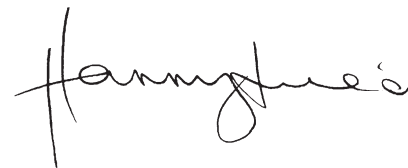
When viewed from this local perspective, many post office closures simply do not make sense. This is because decisions on the shape of the local branch network are being taken at national level - outside of the communities affected. An overly prescriptive national approach means otherwise profitable local branches can be closed because they are crippled by the cost of the national network bureaucracy. Thriving local branches, valued by their communities, are being closed leaving local residents – including vulnerable older people and young families – often with no choice but to catch a bus or drive to other post offices.

Local government has a duty to respond to the needs of local communities. When Post Office Ltd announced in Autumn 2007 that our county would see over 30 further post offices closures we knew we had to act.

Essex County Council has now set aside £1.5 million over three years to keep local post offices open and to help them identify new opportunities to become self-sufficient. In doing this, we are starting to create something which doesn't currently exist – a positive future for the local post office network.

This pamphlet goes further still. It aims to kick-start a debate on the future of the post office network and suggests a model of future provision. It recommends bringing the branch network into the family of local government services and, in doing so, creating a connection between local post offices, local funding and local accountability.

Without a new vision for the post office network, local branches will continue to close and communities will continue to suffer. Therefore, I hope you find this contribution to the debate encouraging and thought-provoking. One thing is certain; if we are to secure the future of the local post office, we need a new way forward.



**Lord Hanningfield**  
Leader, Essex County Council.

## Summary

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Post offices are among our most valuable, and most valued, community assets. As well as providing postal services, local branches provide a resource for local businesses and a centre for public information. In rural villages they are a much needed access point for banking and financial services. Perhaps most importantly, post offices play a vital role in supporting the independence of the most vulnerable in our society. They can help older people to stay active, providing an infrastructure to help them access services in their own communities and helping them live independently in their own homes.

But the post office network cannot be sustained as a wholly commercial enterprise. Post Office Ltd estimates that a fully commercial network could contain only 4,000 of the 13,500 branches currently operating. The government have pledged around £150 million per year to 2011 to keep branches open, but without a new vision for the network, closures will start afresh when these subsidies stop. Even with continued subsidy, changing consumer habits and the loss of key contracts could stretch the post office network to breaking point.

Building on our pioneering work to secure the future of local post office branches, this pamphlet presents our vision for the future of postal services. We propose a split between Post Office Ltd's commercial assets, (its products, national contracts etc) and its main community asset – the branch network.

We propose that the branch network be brought into the family of local government services. Upper-tier and unitary authorities would commission local post office services and shape the network in line with the needs of their local communities. Councils will have a role in improving the efficiency of the local networks too. They could increase postmasters' bargaining power by negotiating contracts on behalf of all local branches; they could shape local provision through innovative local commissioning and partnership arrangements; they can explore the co-location of post office services with other local public services. At the same time, Post Office Ltd will be able to focus on the profitability of their commercial operations – their success determined by their ability to market their products and win commercial contracts.

But our proposal goes beyond improving efficiency and cutting costs. It proposes a model of provision that will secure the future of a valued community service, support the elderly and most vulnerable, and ensure that the future of the local post office branch is not determined in Whitehall or by analysts at Post Office Ltd's head office, but by democratically accountable local councils.

# Introduction

In September 2008, Essex County Council became the first UK local authority to use local funding to reopen a post office branch closed by central government. We did this because we know the important role that post offices play in our communities. We also realise how valuable post offices can be in complementing the work of other local public services – particularly those services providing public information and encouraging independence among older and vulnerable people.

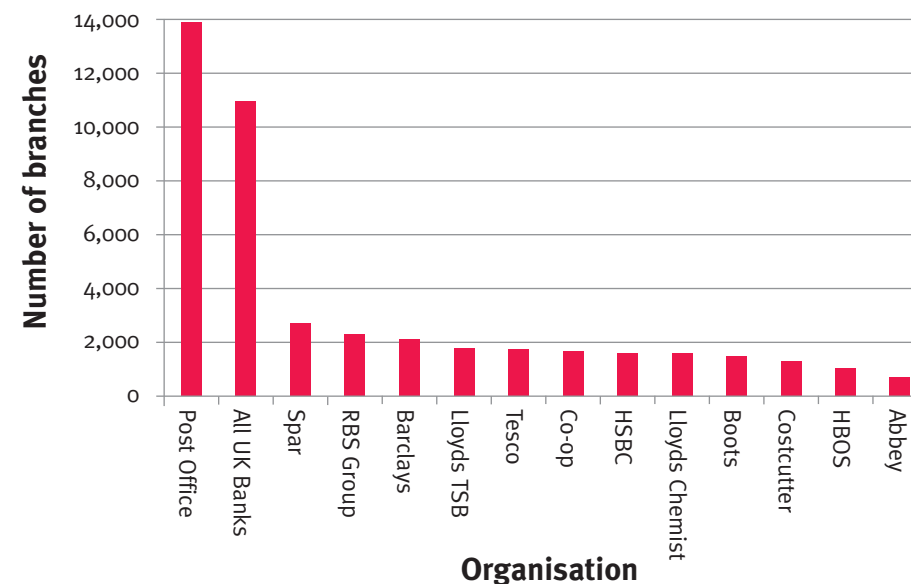
This pamphlet builds on our initial experience – it sets out a new vision for local authority involvement in post office services. It highlights the valuable role post offices play in local communities, traces the decline of the branch network and examines the role played by the present government. It then proposes a new model bringing the local post office branch network under the stewardship of local authorities. This proposal brings the local branch network into a direct relationship with local representation and local taxation. However, it leaves Post Office Ltd's commercial activity squarely in the private sector.

Our aim is to take the debate in a new direction. It is clear to us that the current model of post office provision is not working – commercial constraints are squeezing branches out of their important community role. We hope the debate can lead to long-term sustainability in the post office network and a framework for provision that recognises the importance of both commercial and community imperatives.

## The post office network

Post Office Ltd (PO Ltd), together with Parcelforce Worldwide and Royal Mail, is one of the three domestic businesses that make up the Royal Mail Group. Royal Mail Group is a public limited company with a single shareholder – the British Government. Within this group, PO Ltd runs the UK's post office branch network – the largest retail network in the country with around 13,500 branches. Each branch provides an access point for postal services as well as a range of communications, banking and public information services.

Figure 1: **Size of retail, banking and post office networks**



Source: Post office branch figures are based on Royal Mail Group's Annual Report and Accounts 2007-08, other figures are based on DTI, (2006), taken from DTI, (December 2006), *The Post Office: a consultation document*.

## EssexWorks for Local Post Offices

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In Essex, we are pioneering a new approach to postal services using local funding to secure the future of local branches.

We are looking to develop a local network providing postal services and community information points across a range of small, independent retail outlets. Our approach involves testing outlets against eligibility criteria examining issues such as local need, the availability of alternative services, physical accessibility and the layout of the premises. We then approach eligible retailers to see if they are interested in operating a post office service. Retailers with experience of running services tend to be most interested – but others are keen too!

We then negotiate the shape of the local service in our selected locations with PO Ltd. Where PO Ltd are happy to see services reopen, they conduct their own assessment of potential providers and subject their businesses to detailed scrutiny. Where there is a need to affiliate reopened services with a larger "third-party", or "core" post office, PO Ltd also identify and approve these branches. The process is complex and arrangements need to be carefully explained to potential providers.

We are piloting our approach based on time-limited grants and a mixture of stand-alone services and "core" post offices. Negotiations have been lengthy and we want to be satisfied that our approach will deliver value for money. We have therefore kept funding arrangements as simple as possible. We have given start-up grants to approved providers based on the number of customers, likely transactions and staff they require. On-costs associated with the new post office service have to be met by providers.

We have insisted that providers prepare a business plan and train to deliver both community information services and the usual post office services. Over time, the business plan has to demonstrate how the postal activities contribute to overall trading profit. Where "core" post offices are part of the service model, their business plan and that of the service provider have to take account of the business relationship between the two parties. While independent of the County Council, we support both parties to develop their respective business models.

Essex residents visiting locally funded postal offices see, in effect, a new brand on the high street: independent from PO Ltd with an emphasis on access to community information as much as postal services. Each branch will have an information point offering internet access – an important resource given the relatively low level of broadband access among our target market (older people etc). Postal services play a key part in the network but they need not be provided at every branch. In some instances, the provision of: information points; a free cash point; an electronic payment terminal; and mail collection facilities is all that may be required to meet local need.

We will continue to scrutinise our approach to see how it can be improved and developed in the future. We will continue to ensure EssexWorks for local post offices.

The network consists of two different types of post office branch:

1. Crown offices - those managed directly by PO Ltd (some 390 in total); and
2. Privately owned branches managed on an agency basis by either individual postmasters or a franchise partner such as WH Smith or Budgens.

Crown offices are managed by PO Ltd employees, but privately owned branches are not. Both postmasters and franchisees have a contract with PO Ltd to provide services using their own premises and staff. Most run these services alongside another retail business.

It is hard to overestimate the scale of the post office operation. The company's main clients are the UK government and the Royal Mail who, between themselves, have accounted for as much as two thirds of PO Ltd's past revenues. In 2007-08 PO Ltd's total revenue reached £911 million; the network had some 24 million customers, carried out around 63 million transactions and paid around 390 million bills. Royal Mail Group estimates that 15 pence of every £1 transacted in the UK is handled by the post office network.<sup>1</sup>

## The value of the post office network

Few services are valued as highly by their local communities as the post office. One can gauge the depth of public affection in the reaction to the programme of branch closures. The local post office provides a community service that is greater than the sum of its transactions. The post office helps older and vulnerable residents to remain active and retain independence; it provides access to public information; increases opportunities for social interaction and increases customer footfall for small retailers across Britain.

While the post office is a resource for the whole community, it is perhaps most valued by the old and the vulnerable. PO Ltd's own 'Customer Satisfaction Index' suggests that 99.8% of customers are satisfied with post office services they receive. Analysis from the Citizens' Advice Bureau<sup>2</sup> suggests that 59% regard the post offices as "centres of the community" and cite this as fundamental to their local value. More than eight out of ten see the local post office as a place to get official information, while around two-thirds use the post office as a source of local information and informal advice. The local branch plays a role in promoting financial inclusion too; only 4% of villages have a bank while some 60% have a post office.<sup>3</sup> This is a role particularly valued by older people: many feel safer using the post office as a one stop shop to collect benefits and pay bills, rather than carrying money from one place to the next place.<sup>4</sup> There is also a crucial social dimension – more than a quarter regard the local post office as a place to meet.

This social dimension should not be underestimated - particularly in rural communities. Those rural areas threatened with post office closures are among those who have lost bank branches, shops and petrol stations in recent years. In many cases, the post office is now the only remaining service – an estimated 57% of rural postmasters provide the only retail outlet in their village.<sup>5</sup> The role these postmasters play in their communities – not least in supporting older and vulnerable people – cannot be replicated.

Post office branches also play an important economic role in their localities. Analysis from the New Economics Foundation suggests that the closure of a post office branch has a dual impact on the local economy. There is a direct reduction in the flow of money through the local area as a result of the branch closure,

*"for every £10 earned in income, the post office generates £16.20 for its local economy – of which £6.20 is direct spending on local goods and services."*<sup>6</sup>

And there is an indirect impact on the costs – and therefore profitability – of local businesses,

*"each post office saves small businesses in their direct vicinity in the region of £270,000 each year."*<sup>7</sup>

This indirect impact is considerable. The evidence suggests that 82% of small businesses think that the closure of the local post office would adversely affect their business, increasing travel time, queuing time, and even leading to business closures.<sup>8</sup> Local retailers may bear the brunt. The withdrawal of local branches would increase costs, and can also cut sales through reduced customer footfall.

But it is consumers who will be most affected by post office closures. The branch network has a crucial impact on the quality of life of older and vulnerable people. Post offices can help older people stay active by providing an infrastructure that allows them to access services in their own community. A poll conducted for AgeConcern, suggests that 99% of older people consider their local post office to be a "lifeline" and more than half fear closures would leave them isolated.<sup>9</sup> Indeed, Postwatch Scotland – the consumer watchdog for post office services in Scotland – has estimated that 86% of elderly rural residents would lose their independence if their local branch were to close.<sup>10</sup>

Taken together, the positive impacts of post offices on their communities are considerable. Recent analysis designed to quantify the economic, social and environmental benefits of post office branches in Essex, suggests that six local branches might have a positive impact on their communities worth around £1 million per year (see annex for details). Without this local service, the cost to local authorities of supporting elderly and vulnerable residents could increase by around £61,000 per branch.<sup>11</sup>

## The decline of the post office network

The value of the local post office is palpable, but the network, in its current form, cannot be sustained as a commercial enterprise. PO Ltd currently presides over a network of around 13,800 branches, but estimates that a fully commercial network could consist of only 4,000.<sup>12</sup> The "Network Change Programme" – a Government backed programme of closures – will see the network reduced by 2,500 branches in the immediate future, in the name of improved network sustainability.<sup>13</sup>

But the "Network Change Programme" is not the first round of closures designed to improve commercial sustainability. The "Urban Re-invention Programme" invited voluntary branch closures in urban areas between 2002 and 2005 and around 2,500 branches were closed.<sup>14</sup> Now, within three years of this programme's completion, local post offices face a closure programme of similar scale.

Even with this latest round of closures it is unrealistic to expect the network to survive, at its current size, over the long term. Although PO Ltd have enjoyed some success in developing new commercial products – credit cards, ISAs, foreign currency, travel insurance and broadband to name but a few - the network is still being heavily supported by both the British taxpayer and individual postmasters.

Perhaps the clearest sign that the post office network cannot be sustained as a wholly commercial venture is the scale of financial support it requires from the taxpayer. PO Ltd

effectively receives public subsidy through the "Social Network Payment" – a Government grant to cover the costs associated with maintaining those post office branches that would not be provided by a purely commercial organisation. The Social Network Payment provided revenue of £75 million in 2006-07 and £150 million in 2007-08. Without this payment PO Ltd would have recorded losses of £184 million; even with support from the exchequer, PO Ltd failed to break even.<sup>15</sup>

Figure 2: **Post Office Ltd's five-year profitability**

Financial year	Operating Profit (including subsidy)	Operating Profit (excluding subsidy)	Public subsidy
2007-08	-£34 million	-£184 million	£150 million
2006-07	-£108 million	-£183 million	£75 million
2005-06	-£111 million	-£111 million	-
2004-05	-£123 million	-£123 million	-
2003-04	-£103 million	-£103 million	-

Source: Royal Mail Holdings Annual Report and Accounts 2003-04 to 2007-08. The figures in column 2 (including subsidy) include the Social Network Payment from central government to PO Ltd. Column 3 (excluding subsidy) shows operating profit without the subsidy and column 4 reports the value of the subsidy.

But the problems facing the post office network are even greater than this suggests. The full extent of the problem is masked by the fact that many franchisees currently run branches at a loss. Although running a post office franchise can increase customer footfall and, as a consequence, the revenue generated by a connected retail business, there is often no "profit" to be made in the provision of post office services themselves. The extent to which individual postmasters and franchisees are supporting the network was recognised by the then Trade and Industry Select Committee in January 2005:

*"Government cannot continue to profess its commitment to a viable post office network for the future while at the same time paying the Post Office (sic) less than the going rate for the job."*<sup>16</sup>

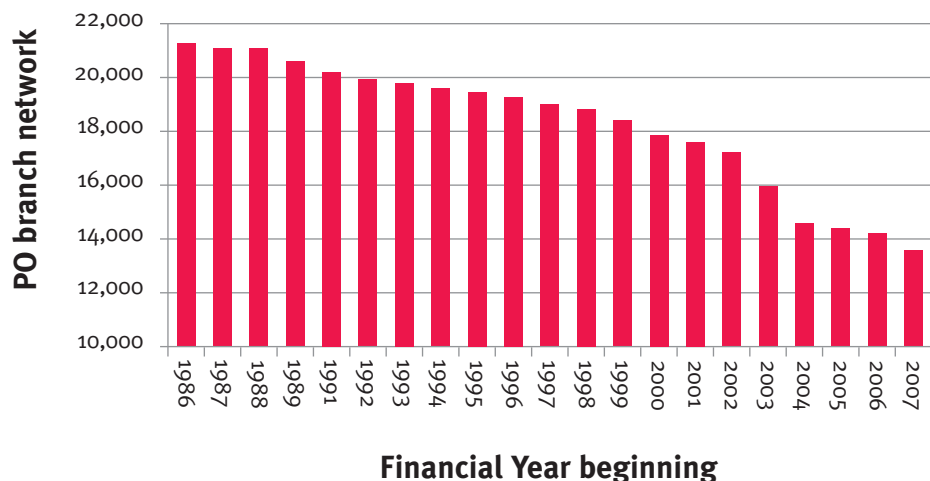
This stems in part from losses made by PO Ltd on central government contracts, but the problem at local level is a complicated system of payments and charges made to local postmasters. Every transaction carried out at a post office brings a fixed commission payment from PO Ltd to the local postmaster. Different types of transactions attract different levels of commission, but most commission payments are set at an unprofitable level. As a result, the basic transaction costs borne by front line postmasters can be greater than the payments they receive.<sup>17</sup>

In addition to this, notional shares of PO Ltd's central costs are allocated to each local post office branch to cover on-costs and other overheads. There is no room to negotiate these allocated

costs and they can exceed those directly associated with providing the service (i.e. the salary and commission paid to the local postmaster). The limited evidence available suggests that, in some cases, only one-third of these overhead charges relate to the support costs associated with the particular branch.<sup>18</sup> As more branches close, it is likely that higher overhead charges will be shared across a smaller number of branches thereby increasing the on-cost each remaining post office has to meet.

The pressure on local postmasters has squeezed the number of post office branches. This has caused the number of branches to decline in every year since at least the mid-1980s. As the pressure on the postmaster increases, more post offices are forced to close; as more post offices close, the pressure on the remaining branches increases further. By 2005-06 the financial viability of post office branches had become the single most common reason for postmasters leaving the sector in rural areas.<sup>19</sup>

Figure 3: Post office branch closures and network 1986-2007



Source: Postwatch, Post Office Network Statistics.

There is little evidence to suggest that PO Ltd will be able to free itself from public subsidy or reduce pressure on local postmasters in the future. If anything, things are going to get worse. Industry analysts suggest that the most significant factor impacting on and undermining the commercial viability of post office branches is the internet. Almost three-quarters of counter services currently offered have been, or are likely to be, replaced by online alternatives. Although many of today's post office customers do not use online services, the numbers who do will increase as today's younger people move into middle age and as tomorrow's older people become more

internet savvy.<sup>20</sup> The implications for the branch network are profound – closures will continue unabated. Analysis from an All Party Parliamentary Group examining the long-term prospects for the UK's 'small retail' sector suggested that post offices in their current form have only a moderate chance of survival beyond 2015. They suggest that without government support, assistance and innovation,

*"...post offices cannot survive despite their importance to local communities. It is believed that the network will be heavily depleted by 2015."*<sup>21</sup>

### The role of central government

The present government has done nothing to halt the decline of the post office network. Its failure stems from an inability to reconcile its role as sole shareholder and major customer: as a shareholder the government is paying subsidies to support the network; as a customer they are undermining the network by cutting its use of post office services.

Much of the post office network's decline can be traced to a loss of revenue from state or state regulated services. The BBC licence contract has been removed from the post office; the number of car tax licences issued in post office branches has fallen following the launch of the DVLA's new web service, and the new European Health Insurance Card has replaced the E111 form, bypassing the post office completely. It is right that all government departments should choose the

most efficient delivery channels for their services, but the repeated withdrawal of business from the post office network has undermined its viability.

But the single biggest blow to the post office network came on 24th May 1999. The government announced that benefit and pension payments would no longer be paid manually over post office counters, but via a more efficient system of direct payments into a bank or building society account. The government hoped to save around £500 million per year but the shift saw the post office network's potential revenue cut by around 40%.<sup>22</sup>

A second significant blow came in January 2006 when it became apparent that the Department for Work and Pensions (DWP) would not be automatically renewing its contract with PO Ltd for the Post Office Card Account (POCA) beyond 2010. The POCA – a basic bank account allowing customers to obtain benefits without using another bank account – had been developed to mitigate the impact of the government's shift to direct benefit payments. Estimates suggest that the POCA allowed the post office network to retain around £400 million in revenue that would otherwise have been lost. If the post office network is to retain this revenue in the future, it must successfully bid for DWP business.<sup>23</sup> There is a very real possibility that PO Ltd could fail to win the second POCA contract. Such failure would seriously undermine the stability of the network even after the current programme of closures. Postmaster incomes could fall by 10%,<sup>24</sup> customer visits could fall by some 6.5 million and branch revenues could fall by £2 billion.<sup>25</sup>

By cutting costs and removing patronage from the post office, the government has further undermined the commercial viability of the post office network. At the same time it has rendered the network dependent on public subsidies. On 14th December 2006 the government announced its latest post office funding package – £1.7 billion to 2010-11. Although some of this will be used to fund compensation for closed branches, ongoing losses and new 'outreach' services, up to £750million has been set aside to support non-commercial branches.<sup>26</sup>

But greater subsidy does not mean greater security – pouring tax revenues into a national bureaucracy will not safeguard local services. The pressure on local postmasters remains and, if the subsidies stop after 2011, the branch closures will start afresh. The impact of this on the independence of elderly and vulnerable groups – and on the public sector care budgets that support these people – could be profound. If government is serious about maintaining the local post office network then a new vision is needed. Essex County Council has led the development of this new vision, and more and more local authorities are looking at ways of securing the future of their local branches. It is time to think about bringing the local post office into the family of local government services.

## A new vision

Let us begin by outlining some basic principles.

- First, any future model of post office provision must recognise post office branches as key community services.
- Second, it must leave room for PO Ltd to succeed as a commercial business.
- Third, we would not want to see private enterprises brought under public ownership.
- Fourth, any new model must improve the long term sustainability of the post office network – we cannot simply change structures and repackage the same problems.

Is there any way to secure the future branch network and respect these principles?

Yes. We propose a radical division be established between PO Ltd's commercial assets – its products (e.g. broadband, ISAs etc) and its national contracts (the POCA) – and its community asset – the branch network. We propose that local authorities become custodians of the branch network giving PO Ltd the freedom to act as a purely commercial organisation.

## A local post office network

We see a role for upper-tier and unitary authorities as custodians of the local post office network. Post offices should become part of the suite of community services councils provide for the adult population. Under the Sustainable Communities Act, the Secretary of State can invite proposals from local authorities wishing to promote the sustainability of their local communities by transferring public service functions from one public agency to another. In the spirit of this Act, we propose that local authorities take responsibility for maintaining and sustaining a local branch network in line with the needs of their communities.

Upper-tier and unitary authorities would take the lead in commissioning new post office services from new postmasters and managing existing contracts with incumbents. The commissioning of local post office services would therefore follow the same rules that apply in commissioning any other local public service. All procurement would, of course, be conducted in line with national and European regulations, including those regarding state aid.

Local authorities and local partnerships would shape the post office network to meet local needs - innovating with contracts and commissioning arrangements to create appropriate incentives for local postmasters. For example, local authorities might make reward payments to local postmasters who increase benefit take-up amongst elderly and vulnerable groups. They may pay bonuses to postmasters who innovate to support the independence of their older and most vulnerable customers.

With a strategic overview of the branch network, local authorities will be able to shape the network by varying the mix of provision according to needs, circumstances and resources. Authorities may seek to commission and support outreach services in rural areas; in deprived urban settlements they may support the survival of franchised offices through more favourable contracts. Authorities may use their relationships with larger businesses and encourage them to sponsor local branches – perhaps running these at cost as part of their Corporate Social Responsibility programme. Local authorities may themselves choose to support un-commercial branches where community benefits have been identified and where the risk of undermining the viability of other local enterprises is minimal.

Local authorities should take responsibility for directly managed Crown Offices at least in the short-term. We believe private franchise arrangements will offer the most sustainable solution for the network. However, decisions on the balance between public and private provision should be made at the local level.

By bringing the strategic management of the local post office network into the family of local government services we will unlock substantial community benefits. But perhaps most important is the fact that local authorities will bring legitimacy to the management of the network. Decisions on the future of the network will be taken away from analysts in PO Ltd's head office and placed in the hands of democratically elected and publicly accountable local leaders.

Only local authorities have the depth of local knowledge required to understand the community benefits of post offices.<sup>27</sup> Local authorities can link decisions on the local network with decisions on care provision, public transport, local economy, and access to alternative services. Most importantly their range of public service responsibilities means they can identify the branches on which local businesses and older and vulnerable residents depend. PO Ltd's substitute for this local knowledge – their "access criteria" – has proved a blunt tool for assessing need. The criteria are not sensitive to local circumstances but instead state baldly that 99% of residents must live within 3 miles of a post office branch. An example of the short comings in this approach was seen in LB Hammersmith and Fulham. After PO Ltd earmarked the Askew Road branch for closure they confessed they did not know about the fifty flats for blind and partially-sighted residents near the branch.<sup>28</sup> Thankfully, after intervention from the responsible Cabinet Member, PO Ltd reversed its decision.

Local authorities also have experience in advising and supporting local business. Local authorities and "Business Link" provide a range of services to local businesses - advice and consultancy, help with sourcing finance, exploring new business and technology opportunities and developing their workforce. A recent survey in Essex suggested that local businesses view the work of the authority as helpful in promoting the county, its tourism economy and the advice and support available through the trading standards service.<sup>29</sup> Local authorities are well placed to extend their responsibilities and provide assistance to un-commercial post office branches.

As community leaders, local authorities are more than just providers and commissioners of services. They play a central role in convening and leading local partnerships. This role would be a significant advantage when integrating the post office network with the range of public and community services. Local authorities can continue to explore opportunities for franchised offices and outreach provision with private partners and third sector bodies. To date progress has been slow in engaging voluntary organisations, charities and community groups to provide postal services; however, local authority leadership, through knowledge of existing networks, will provide new impetus. In this way, the post office network can become a crucial vehicle through which both public and community sector priorities are delivered.

Partnership working, at its best, can improve the quality of local services by exploiting synergies between different types of service. Co-location of services is often the most visible and effective way of achieving this. In Essex, the successful co-location of Braintree District Council's area office with Witham library provides an example. This move has increased the use of library services by 20%, extended the district office's opening hours in response to local consultation and helped rationalise district accommodation.<sup>30</sup> As far as post offices are concerned, many local authorities have already brokered successful co-location initiatives – in pubs, hotels, bed and breakfasts, village and church halls, and village shops.<sup>31</sup> Our new vision could see these isolated examples of innovation become the norm.

## Post Office Ltd

Under this new localist model, PO Ltd will be free to focus on the profitability of their commercial operations – governed by their success in marketing products and winning commercial contracts. There are good prospects for success; Post Office Financial Services – in its joint venture with the Bank of Ireland – was the fastest growing financial services provider in the UK last year. Having launched its financial products four years ago, there is vast commercial potential in the Post Office brand.<sup>32</sup> And PO Ltd's success is not limited to its banking products; one in every fifty car insurance policies are purchased through PO Ltd, it insures one in every two hundred homes and is the largest independent provider of travel insurance in the UK. This, together with success in marketing foreign exchange services, broadband and communications products, suggests that PO Ltd can successfully run its commercial operations without public support.

PO Ltd would be expected, in consultation with local authorities, to prepare competitive bids for national contracts tendered by central government - such as the Post Office Card Account. Successful bids would go some way towards maintaining what has historically been a rich revenue stream for PO Ltd. They will also help maintain the role of the local post office branch in providing a gateway to national public services.

Transferring the branch network to local authorities will not affect PO Ltd's retail provision. We would propose – at least in the medium term – that the local post office network exclusively sell PO Ltd's commercial products. We would hope to enshrine this agreement in contractual terms specifying, on behalf of local branches, PO Ltd's commission structure and, on behalf of PO Ltd, the service standards and level of provision that would be expected of branches.

We would envisage PO Ltd providing supporting infrastructure services (e.g. secure cash transit) under contracts with local authorities and local branch networks. With time however, we would hope to see these contracts opened to the market.

### Financing local networks

One might ask why anyone in local government would want to see the post office network brought into local authorities' remit. Without support from the exchequer to the tune of £150 million, the PO Ltd would have made a loss of £184 million in 2007-08 – why would any council leader or chief executive want to take this on?

The first point to note is that, shared across the local government sector, this is not a substantial sum – no more than 0.34% of any authority's net current expenditure.<sup>33</sup> In the same financial year that PO Ltd recorded these losses, net current expenditure among English authorities alone totalled more than £106 billion.<sup>34</sup> The PO Ltd's losses represent less

than 0.2% of this spending – they could be easily covered by an average local authority Band D council tax increase of less than 20p per week.<sup>35</sup>

Even so, the visibility (and resulting unpopularity) of the council tax together with intensifying pressure on local services mean we cannot reasonably expect councils to shoulder this burden using only their current resources. Nor should we expect them to do so. Central government has already signaled a commitment to maintaining the non-commercial post office network and has set out a funding package worth £1.7 billion to 2010-11. £750 million of this has been set aside to continue the 'social network payment' to subsidise non-commercial branches – the remainder will fund compensation payments to out-of-work postmasters and new 'outreach' services.

With local authorities as stewards of the post office network, we would expect to see current subsidies redirected to councils as part of their formula grant package. Formula grant calculations are notoriously opaque<sup>36</sup> but are based – at least in part – on assessments of councils' relative 'need to spend' on different types of services (social services, cultural services etc). We would expect to see current post office subsidies redirected following similar assessments of councils' need for post office services. Now is not the time to dwell on the intractable problem of local government finance (we have made our case on this elsewhere)<sup>37</sup> but suffice it to say these payments should not be ring-fenced or accompanied by restrictive reporting requirements.

## Generating local savings

Central government grant payments will, without reform of the local financial system, continue to play a major role in sustaining local post offices, at least in the medium term. But the very act of separating the branch network from PO Ltd's commercial operations will lead to local savings and will improve the network's financial sustainability. The separation will change the relationship between the branch network and PO Ltd's supporting infrastructure.<sup>38</sup> What is currently an 'internal' relationship between two parts of the same company, would become a relationship between two parties in the marketplace. This will separate the costs that arise directly from providing services at a given branch from the overhead costs associated with supporting infrastructure. While the former will be met directly within a locally managed network – by postmasters and perhaps by local authorities – the latter will be reflected in the charges PO Ltd levy on local networks through contracts for supporting infrastructure services.

The crucial point is that the separation will exert a downward pressure on infrastructure costs. PO Ltd have been heavily criticised for the lack of clarity in the overhead cost charges to individual branches.<sup>39</sup> By bringing these figures into the open, we can ensure that every branch pays a fair price for the infrastructure services they consume.

The downward pressure on overhead cost charges would be intensified as local authorities increase the bargaining power of their local postmasters. At the moment, PO Ltd negotiates overhead charges on a branch by branch basis (if at all). With councils overseeing their local network, they can act as a single interface with PO Ltd, negotiating terms on behalf of all their branches and exerting further downward pressure on overhead charges. The success of PO Ltd's infrastructure business will, like every other private enterprise business, depend on their ability to provide competitive services at competitive prices.

It is worth noting that increased transparency in PO Ltd's finances is valuable for its own sake too. MPs have recently raised the issue that Royal Mail could be paying PO Ltd less for mail services than would be necessary to support PO Ltd's profitability. They have raised the possibility that public subsidies to the post office network could, in effect, be subsidising Royal Mail's commercial mail business.<sup>40</sup> Separating the publicly-supported branch network from PO Ltd's commercial contracts would eliminate any such risk.

## Local innovation and local efficiency

Overheads and infrastructure costs are not the only areas where we might expect savings to accrue as a result of local authority involvement. Local councils have an established track record in improving efficiency through local innovation and partnership. In the first instance, and as outlined above, we would expect to see local authorities move towards franchise arrangements for existing 'Crown Offices' – branches that are directly managed by PO Ltd's bureaucracy.

Franchising offers the best chance of survival for Crown Offices and provides clear opportunities for network cost reduction.<sup>41</sup> Crown Offices currently lose an average of £127,000 per branch per year because of high property costs, high overhead costs, high wage bills and falling incomes.<sup>42</sup> Postcomm – the postal services regulator – observes that Crown Offices

*"have a reputation for being very expensive to run and for being a major contributor to Post Office Ltd's losses".<sup>43</sup>*

But the current process for converting a Crown Office to a more profitable franchised branch is onerous and slow. PO Ltd must advertise for prospective franchisees, applicants are then subject to a registration and vetting procedure and are then required to submit a business case for the particular branch they wish to run. PO Ltd then interviews applicants who satisfy its selection criteria before making a decision.<sup>44</sup>

Local authorities have the local networks and the knowledge to franchise local branches quickly and successfully. PO Ltd managed to convert only 283 Crown Offices to franchise arrangements between 1994 and 2004 but it will need to convert an additional 230 between 2005 and 2010.<sup>45</sup> Local authorities can increase this conversion rate and reduce local costs whilst ensuring provision remains in line with local needs. Local authorities already play a substantial role in building local partnerships and commissioning local services. Councils convene partnerships from the local business community, the wider public sector and voluntary and community sectors not just because of their formal responsibilities, but as an inevitable consequence of their position in local communities. These partnerships have a track record of innovation that could help to accelerate the process of post office franchising, giving loss making branches a sustainable future in the private or voluntary sectors.

Where Crown Offices cannot be migrated to franchise arrangements, local authorities can innovate and reduce costs in other ways. Perhaps the most significant opportunity comes from the co-location of the post office branch with other public services. Post office branches are only one of the range of local public service outlets that include libraries, schools and colleges, GP surgeries, benefit offices etc. Local authority partnerships can bring opportunities for co-location and cost sharing which PO Ltd cannot hope to achieve in isolation.

## Making it happen

We are confident that an ambitious local government sector can provide a sustainable future for local post office branches. But we know they cannot do this alone. The £150 million ‘social network payment’ reduced PO Ltd’s £184 million loss to £34 million in 2007-08 and financial support from central government will be needed in the medium to long term.

A fully costed model lies beyond the scope of our paper – we doubt whether sufficiently robust financial figures exist to allow us to prepare such a model. However, it is not inconceivable that by making branches’ overhead charges clearer, by increasing postmasters’ bargaining power, and by allowing local partnerships to innovate, the UK’s local authorities could overcome PO Ltd’s current losses of £34 million.

But bringing the post office branch network into the family of local government services will do more than simply cut costs. It will help support the elderly and most vulnerable in our society and will secure the future of a valued community service. It will also bring the local post office into a direct relationship with local democracy and local taxation. Councillors can shape the local network to meet local needs and preferences. Any network changes will be constrained – at least in part – by the competing demands placed on local tax revenues; they will be influenced and perhaps even determined by local wishes expressed at the ballot box. We are confident that our proposal offers a sustainable future for the post office network, a future based on a vision of locally responsive services delivered by democratically accountable leaders.

## ANNEX

# Quantifying the Community Benefit of Essex Post Offices

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## Purpose

This paper summarises analysis designed to quantify the "community benefit" of Post Office branches in Essex. The paper summarises methodological considerations, the model used to derive estimates and the key assumptions that underpin the analysis.

We will continue to develop and refine our model over the coming months.

## Scope

Our estimates are based on our investigation of the role and value of a sample of six post office branches in Essex communities<sup>1</sup>. Our objective in developing these estimates was to quantify (in financial terms) the non-financial benefits derived from these post offices and enjoyed by the community (greater independence for older people, reduced care costs etc). The notion of ‘community benefit’ occupies the same conceptual space as the economists’ ‘positive externality’. They include the benefits that accrue to the community from the role post offices play, but do not include wholly private benefits enjoyed by individual customers or by postmasters.

Working within this conceptual framework means we are not concerned with quantifying the costs that might accrue to particular public or community sector budgets as a result of any policy decision – e.g. the decision to open or close a

particular post office branch. Our estimates should be regarded as indicative of the community value of local post offices rather than as definitive financial statistics.

## Context

It is important that our estimates are viewed in context. There is no direct source of data on the community value of local post offices. We therefore:

1. constructed a quasi-financial model;
2. formulated assumptions about local Post Offices, local businesses and local behaviours; and
3. derived estimates of "community benefit" on different scenarios.

Our approach has been informed by similar and related studies in the current literature. Where similar work has been completed, it tends to follow one of two approaches. It is either:

1. based on a willingness to pay – survey questions have been used to ask respondents how much they would pay to maintain or reopen a local service in their area;<sup>2</sup> or

<sup>1</sup> *We have not identified the six specific post offices as Essex County Council's negotiations with these Post Offices are ongoing.*

<sup>2</sup> *For a good example in the debate around Post Office closures see NERA Economic Consulting, (August 2007), Access to Postal Services. Postcomm.*

2. based on the cost of providing alternatives – analysts highlight the value of a local service in terms of the cost of the next most desirable alternative.

Both methodologies have their difficulties. The primary difficulty with the "willingness to pay" approach is that survey respondents report substantially different amounts to maintain local services threatened with closure than they do to reopen previously closed services. Whilst the main conceptual difficulty with the "cost of alternatives" is that it can assume the financial cost of the alternative reflects the full community value. This is a problematic assumption given that the overall analysis assumes that the financial costs of current provision do not fully reflect these benefits.

Given these potential difficulties we have constructed a mixed-methodology model made up of modules covering different dimensions of community benefit.

## Findings

The estimates of the community value of the six post offices are summarised in Table A. All estimates are reported at 2007-08 prices and relate to the benefits we would expect the community to enjoy in any given year. The method we used to derive these estimates allowed us to construct three scenarios based on pessimistic, realistic and optimistic assumptions.

Table A: **Community value associated with six Essex post offices, 2007-08**

Category	Pessimistic assumptions <sup>3</sup>	Realistic assumptions	Optimistic assumptions
Economic benefit (indirect) <sup>i</sup>	£128,081	£334,560	£619,436
Economic benefit (direct) <sup>ii</sup>	£220,948	£277,899	£358,280
Environmental benefit <sup>iii</sup>	£130	£514	£1,329
Older People: Social isolation <sup>iv</sup>	£89,580	£179,160	£268,740
Older People: Health and Care <sup>v</sup>	£92,294	£184,589	£276,883
Total	£531,034	£976,722	£1,524,668

i This module mirrors, in broad terms, a local impact model (LIM) used by the New Economics Foundation in their 2006 study on the economic impact of post office closures in Manchester. The LIM can be understood as quantifying the economic impact of Post Office services on the business community surrounding Post Office branches.

ii This module builds on a three-phase local multiplier model (LM3) used by the New Economics Foundation in their 2006 study on the economic impact of post office closures in Manchester. We have developed this model to estimate: the reduction in the flow of money resulting directly from the closure of post office services, and the reduction in the flow of money resulting from a reduction in trade at the retail outlet hosting the closed post office counter.<sup>4</sup>

3 Our model makes explicit the assumptions we make under each scenarios.

- iii This module quantifies a very narrow set of environmental benefits – those which accrue to the community as a result of reduced car use. This is estimated by the cost of offsetting the carbon resulting from the extra journeys that would be undertaken if the post office branches were closed.
- iv Post office branches play a role in helping people enjoy social contact. This is particularly true of those who are vulnerable and elderly. This module quantifies the benefits of this role to the community based on estimates of the cost of alternative ‘befriending’ services.
- v Post offices can help older people to stay active, reduce the demand for social care packages, and by providing an infrastructure that can help older people to access service in their own communities, can help them remain in their own homes rather than residential care. This module quantifies the financial benefits of helping older people to stay in their own homes.

### Investing in Essex post offices

We are confident that our estimates can play a legitimate role in informing investment decisions. Essex County Council recently pledged £1.5 million over three years (£500,000 per year) to support local post offices and to help them find ways of becoming self-sufficient.

Our analysis suggests if Essex County Council (ECC) were to invest £1.5 million in maintaining the six Essex post offices included in our analysis, the community benefits would exceed the investment on even our most pessimistic assumptions. For every pound invested in maintaining these post offices, Essex could realistically expect to deliver around £1.95 in benefits to the community.<sup>5</sup>

4 This approach allows us to account for the fact that although no host retailers are planning to close when the six post office counters are de-commissioned, their retail turnover will suffer as a result (e.g. through reduced footfall). The NEF’s Manchester study assumed that the whole enterprise would close.

The rationality of individual investment decisions will, of course, depend on the circumstances of individual post office branches – the composition of the local economy and the number of older and vulnerable people nearby. The community benefit delivered by individual post offices varies significantly (see Table B) and it is therefore reasonable to expect ECC to target investment in post offices where the benefits to older and vulnerable people and the economic benefits are greatest.

It should be noted that community benefits are only one element of the overall set of benefits associated with investing in local post offices branches. ECC achieved an estimated £6.7 million pounds worth of publicity as a result of its post office initiative.<sup>6</sup> Although we would not countenance community investment decisions being justified on this basis, we might expect this to have a positive impact on residents’ engagement with the council as a community leader. Similarly there are benefits in associating the ECC brand with the Post Office branch. These benefits are difficult to quantify, but based on a Bank of Ireland valuation, the Post Office brand was worth some €44,000,000 in 2005.<sup>7</sup> We might expect this ‘brand association’ to be worth a further £2,500 to £3,200 per post office to ECC.<sup>8</sup>

5 Based on the assumptions underlying our ‘realistic scenario.’ On the basis of our ‘pessimistic’ assumptions, ECC could expect to deliver £1.06 for every £1 invested. Based on our ‘optimistic’ assumptions it could expect to yield £3.06.

6 Essex County Council Communications directorate – based on the value of equivalent advertising space and adjusted to reflect editorial control.

7 Bank of Ireland, (2005), Annual Report 2004-05.

8 Based on a pro-rata distribution of brand value across all post office branches in the UK network.

Table B: **Community benefit by post office (2007-08 prices)**

Post Office*	Pessimistic assumptions	Realistic assumptions	Optimistic assumptions
‘Most valuable post office’	£132,224	£240,355	£371,379
‘Least valuable post office’	£38,233	£76,618	£128,430
Sample average	£88,506	£162,768	£254,111

\* Average figures should be treated with extreme caution. This sample of six post offices is not necessarily representative of all Essex branches. There is substantial variation around this average (up to 57%).

# References

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- 8 Federation of Small Businesses, (December 2006), *Small Businesses and the UK Postal Market*.
- 9 Age Concern consulted 675 people over 60, living in a rural area, between 1 August and 15 September 2006
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- 14 See Postcomm, (October 2005), *Review of the Urban Re-invention Programme*.
- 15 Royal Mail Group, (May 2008), *Annual Report and Accounts 2007-08*.
- 16 House of Commons Trade and Industry Select Committee, (January 2005), *Crown Post Offices, third report of session 2004-05*. HC 91-1. See also Memorandum submitted the House of Commons to Business and Enterprise Committee by Friends of Rippingdale Post Office on 5th March 2008, and Memorandum submitted by Save Tilton Post Office Campaign.
- 17 See Postwatch submission to the Trade and Industry Select Committee, May 2003, quoted in New Economics Foundation, (December 2006), *Last Post: the social and economic impact of changes to the postal service in Manchester*. Also see letters to the House of Commons Business and Enterprise Committee from Naomi Nardi, *Bridestowe Post Office & Riverside Stores* dated 30th May 2008 and 22nd June 2008.
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- 19 Post Office Ltd, *RTA assessment of resignation reasons (rural only)*, quoted in Postcomm, (October 2007), *A Sustainable Customer Focus Network, seventh annual report on the network of post offices, 2006-07*.
- 20 Analysis by the Triangle Management Services, quoted in New Economics Foundation, (December 2006), *Last Post: the social and economic impact of changes to the postal service in Manchester*.
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- 27 When Alan Cook, Managing Director of PO Limited, was asked in the Business & Enterprise Committee what the Essex County Council got out of keeping post offices branches open other than keeping his business open, he replied "nothing" . See House of Commons Business and Enterprise Committee, (July 2008), *Post Office Finance: matters arising from evidence taken on 10 June 2008*. HC 662.
- 28 See [http://www.lbhf.gov.uk/Directory/News\\_and\\_Media/The\\_Leader\\_page/Share\\_your\\_views/93980\\_Hot\\_Topic\\_post\\_office\\_closures.asp](http://www.lbhf.gov.uk/Directory/News_and_Media/The_Leader_page/Share_your_views/93980_Hot_Topic_post_office_closures.asp) accessed on 18th August 2008.
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- 30 Other examples include Ebbisham Centre, Epsom & Ewell; the library includes a Learning Centre and is on the 1st floor of the Ebbisham Centre which includes a lifestyle centre (gym and exercise facilities) and Medical Centre (<http://www.theebbishamcentre.org.uk/>). The Braintree Children's Trust in Essex; a multi-agency, co-located team providing services to children and young people aged from 0 to 19 and their families in the Braintree District (<http://www.idea.gov.uk/idk/aio/6441806>). Cambourne Library in Cambridgeshire; this shares its building with Monkfield Medical Practice, Trading Standards and the Police, and library staff act as building receptionists for these partner Organisations ([http://www.cambridgeshire.gov.uk/NR/rdonlyres/9FAD9E03-B5F8-49B6-B2A1-1B49E6F917F3/0/cambourne\\_profile.pdf](http://www.cambridgeshire.gov.uk/NR/rdonlyres/9FAD9E03-B5F8-49B6-B2A1-1B49E6F917F3/0/cambourne_profile.pdf)). The Idea Store in Tower Hamlets: where adult education classes, library services, events and a café are all co-located in single buildings (<http://www.ideastore.co.uk/>).
- 31 Examples include Parton Village Hall in Cumbria that houses Post Office service two mornings a week, Sheepy Magna Church in Leicestershire which hosts a post office service from the church vestry in the tower base - see Commission for Rural Communities (12th June 2008) News Release: Rural disadvantaged must not lose out from changes to post office network.
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- 38 This supporting infrastructure might include back office services such as transaction processing, security, cash-in-transit services, information technology and marketing.
- 39 For example see, House of Common Business and Enterprise Committee, (June 2008), *After the Network Change Programme: the future of the post office Network*. HC 577.
- 40 House of Commons Business and Enterprise Committee, (July 2008), *Post Office Finance: matters arising from evidence taken on 10 June 2008*. HC 662.
- 41 Some parties have expressed reservations about the stability of franchised provision, but there is little evidence to support this view. PO Ltd report that of 128 new conversions from Crown to franchise branches, 125 franchisees chose to renew their contracts, some for a third time.
- 42 See House of Commons Business and Enterprise Committee, (January 2005), *Crown Post Offices*. HC 91-1.
- 43 Postcomm, (August 2002), *Access to Postal Services*.
- 44 See House of Commons Business and Enterprise Committee, (January 2005), *Crown Post Offices*. HC 91-1.
- 45 *Ibid*.