



MODERN - ISATION BY CONSENT

A Royal Mail for Everyone

compass

DIRECTION FOR
THE DEMOCRATIC LEFT

Modernisation by Consent

A Royal Mail for Everyone

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Executive Summary

- The government wants to modernise Royal Mail. So do we. The problem is that it has ended up proposing to part-privatise Royal Mail; but there are other, better routes to modernisation.
- Instead of privatisation the government should look to its own best practice in the reform of institutions like the BBC and the creation of Network Rail to develop modernisation of Royal Mail within the public sector and with the consent of all the organisations' key stakeholders: the management, the workforce and the public who are its customers. At the moment there seems to be little if any appetite amongst these three groups for privatisation; amongst the workforce and the public there is strong opposition. This seriously jeopardises the chances of success of modernisation through privatisation.
- The government operates under the mistaken view that Royal Mail is somehow a commercial basket case. It isn't. In the first three quarters of this financial year it made £225 million. It did this while charging some of the lowest prices in Europe. It would have made a lot more if it didn't have to fund the pension deficit and in effect subsidise private sector providers through lower-than-cost access charges. When these two issues are dealt with, then Royal Mail will start to make much bigger profits, which can be used to modernise the whole organisation.
- The government has also got into a political mess. Because of the scale of dissent on the Labour backbenches they will need the support of opposition parties to get the legislation through. But the Tories can't be trusted and are likely to spring a trap by demanding more than a minority sale in return for their support once it reaches the Commons. The government will then be on the hook of being 'saved' by the Conservatives or see the legislation defeated.
- But the Post Office union, the Communication Workers Union (CWU), is in a bind too. Simply defeating the legislation is not enough – as the Tories are likely to be in power in a year and will privatise the whole lot with no concessions.
- So both sides need a long-term solution based on the votes of Labour MPs. This document attempts to set out a route map for the government and the union to do a deal that works in everyone's interests – primarily those of Royal Mail's customers.
- There need to be solutions to the pension deficit and investment in new technology. We think both issues can be dealt with quickly and easily. The real sticking point is industrial relations. We know that the government sees the union as a problem, a road block to reform.

- That view, as we will explain, is unjustified. But even if the strength of the union were a central problem and could be broken – what purpose would it serve? Royal Mail is not like the print industry, for example, which was reconfigured by breaking the power of the print unions through the implementation of new technology. Clearly there needs to be investment in new IT and some jobs will inevitably be changed and lost. We think the union accepts this. But Royal Mail and its delivery and sorting system is always going to focus around people, and their commitment and participation in ongoing reform. So change, if it is to be effective, cannot be done to them but only with them.
- Nothing other than consent will work for this historic institution. An imposed solution will just continue the old disputes in a new guise. To improve industrial relations the government can, once again, look at its own good track record in education and health service reforms and apply the same or similar models to Royal Mail. In both cases troublesome industrial relationships were resolved, to the ultimate benefit of the people using those services.
- More than anything Royal Mail needs a fresh start and the ability to go forward in a united way to build a world class public organisation. That demands a new structure: new management with the appropriate transformational skills, fresh investment from outside the government's borrowing limits and the ongoing commitment of the workforce and the union to modernisation. All of this can be achieved within the public sector.
- Our aim is to see a restructured and modernised Royal Mail and Post Office Ltd as a not-for-profit body with improved services under a new model of public ownership.

There are two sections of this report. First we explain the reasons why privatisation is not the right future for Royal Mail; then we suggest a range of governance, investment and industrial relations reform measures the government and the union should consider, enabling modernisation by consent. The detail should then be left to them to thrash out, but this document provides a framework. These are the key conclusions:

1. Royal Mail needs a fresh start: a new structure, and outside managers who can transform the business and create an effective partnership with the workforce.
2. The union must recognise that this entails a fresh start for them too. They have to step up to the plate and offer a constructive basis for ongoing reforms that serve the public interest.
3. Royal Mail is not the failed and failing organisation portrayed – it is the lowest priced service in Europe and is profitable across all areas of its operation. It can be made even more profitable in the public sector when the pensions and access charging issues are dealt with.
4. The pension deficit is in part a consequence of the 13-year pensions 'holiday' given by the government to Royal Mail. The government has generously accepted its

responsibility by taking over the deficit. To nationalise this debt while privatising the profitable Royal Mail would alienate the British people.

5. Any weaknesses in Royal Mail's service have been caused by lack of investment, political interference, unfair regulation and the last government's decision to give £2.4 billion of Royal Mail profits to the Treasury.
6. Going ahead with privatisation now is wrong not just in principle but also in practice. Because this is the bottom of the market the Treasury would get around £1 billion, little more than half the sale revenue that it would have made if it had sold just a year ago. If it remained in the public sector, without the pension deficit and fair access charges, Royal Mail could be making over £600 million every year, money that would be wholly reinvested in the service. The government needs to ask itself the question 'why now?'
7. There are good existing models for a new Royal Mail governance structure. We suggest looking at Network Rail (the successor to a previous disastrous privatisation), which is run as a not-for-profit organisation, with access to both government and private financing. It is operationally free from government, has the efficiency of a united and holistic infrastructure, with strong private sector managements and the ability to borrow on the open market without affecting the government debt. Other models with features that would apply to Royal Mail are the BBC and Welsh Water.
8. Industrial relations in Royal Mail need to be improved. The blame game is unproductive. Ending the threat of privatisation would be the starting point of a new relationship between managers and the workforce. Models such as the Agenda for Change in the NHS could be usefully applied to Royal Mail. It has allowed harmonisation of conditions of service, freedom for employers to focus on best outcomes for patients, and a transparent pay and grade system for employees, which recognises and rewards their skills and competencies.
9. Based on a new governance model, fresh investment and improved industrial relations modernisation should then include developments like a fully formed People's Bank based on the Post Office network, hybrid mail, new services linked to internet trading, same day urban deliveries, timed and tailored deliveries as well as home collections.
10. All of this only works as a package within the public sector. Enabling a new publicly accountable entity provides the basis for a fresh start, opens up investment, which is boosted further by solving the pension issue, and creates the conditions for a partnership between all Royal Mail's stakeholders.
11. Governments are remembered by the new institutions they leave behind. The present government could be remembered for saving our great national postal service, modernising it by consent, and therefore creating a future proof Royal Mail that is both popular and efficient. By taking the route suggested by this report, the government would show that far from being exhausted it understands that traditional values need to be delivered in a modern setting. What could be more New Labour?



We don't want to have to campaign against price increases and branch closures or against job losses and worsening terms and conditions for the postal workers on whom a great service depends.

I. Introduction

Britain needs the best possible service from Royal Mail and the Post Office. It plays a unique role in the social and economic life of the nation. Every citizen comes into contact with it virtually every day. For all business life, but especially small and medium size enterprises, it is a vital life line. And beyond all the functional importance it is one of those rare institutions that still says something about who and what we are as a nation. It is iconic.

And yet it has been neglected. Successive governments have refused to invest in it sufficiently and have instead both liberalised the system and hovered, waiting for the right opportunity to sell all or some of it off. It is unsurprising that in such a climate relationships between the management and the union have been poor. It's amazing the service has coped at all.

With echoes of 1994 when Michael Heseltine tried the same move, the government has decided that to be 'saved' Royal Mail needs to be part-privatised. It arrived at this point with the help of the Hooper Report,¹ which argued that because the service needs modernisation and therefore more investment, the pension deficit needs to be dealt with and an unhealthy industrial relations record needs to be put right – the only response was part-privatisation.

We agree with much of the analysis of Hooper, although as we have shown he overstates the weaknesses and failures of the organisation.² Royal Mail and the Post Office need to be modernised; there needs to be a change; new investment needs to be secured; and the relationship between management and employees requires a fresh start. But we totally disagree that privatisation, even in part, is the answer. Privatisation would break up the service, spilt Royal Mail from Post Office Counters and cause huge inefficiencies. Money would start to leak out of the system to private shareholders, and any substantial part sale of the service, giving the new management a strategic shareholding, would mean that the service is run primarily for profit and not for people. Crucially it would not solve the industrial relations problems but embed them; a resentful workforce and union is no basis for a people-to-people service.

The experience of the banking sector shows where this can lead. We don't want to be back in a few years' time with a campaign to halt the bonus culture of the new bosses of a privatised mail service. We don't want to have to campaign against price increases and branch closures or against job losses and worsening terms and conditions for the postal

workers on whom a great service depends. We don't want to have to demand a windfall tax on the excess profits of the new owners, only to be told that they are registered abroad and don't have to pay any tax at all.

We believe instead that Royal Mail and the Post Office can and must be modernised as a public body that is wholly not for profit. This report makes the case for why and how.

It starts from the view that the status quo is not an option. The service we get from Royal Mail and the Post Office is still very good and much better than Hooper would have us believe. Delivery standards are high compared with other countries and prices very low. The organisation is making a profit and could make more for investment if it is kept in the public sector. But there has to be change, especially in an era of new technology and new consumer and global demands. But it must be the right kind of change. Modernisation isn't necessarily benign. We should recall that Thatcher was a moderniser. So it has to be the right kind of modernisation. Today, none but the most blinkered politician would argue that privatisation is the only form of public service modernisation.

Instead of privatisation, Compass would like to see a new model of ownership for Royal Mail and the Post Office – one that isn't about private profit, that builds a strong and enduring partnership between the management, the staff and the union, which allows for fresh investment and which results in a better service for all.

To achieve that we examine a number of models already in existence and argue for the best elements of each to be applied to a new Royal Mail – one that serves the public but is independent of political interference, has a new industrial relations culture and the resources to modernise itself effectively. In this way we can apply our enduring values of liberty, equality and solidarity to new and challenging circumstances. We want to see a situation in which the power and strength of the workforce and the union are not broken but redirected away from disputes with the management based on the fear of privatisation or liberalisation without investment, towards the process of modernisation and service improvement.

Time is short though. The government has introduced its proposals in the Lords before they go to the Commons. But there is a dilemma that plays on the minds of both the government and the anti-privatisation coalition, that unless constructively and imaginatively addressed will impact damagingly on the end user, the British public. It is this. The government we hope and expect does not want to pass such controversial legislation with the help of the Tories. Then David Cameron will look as if he is coming to the rescue of a beleaguered Prime Minister. This will only serve to undermine the re-election hopes of Labour further. Indeed, Labour ministers must know in their hearts that they can't trust the Conservatives who, at

the last minute, may well demand a majority sale in return for their support. A Labour leader, just one year away from re-election, cannot be seen to rely so heavily on his opponent.

But the union faces a problem too. It may have sufficient backing in the Parliamentary Labour Party to force the government to stop in its tracks – presuming there is no deal with the Tories. With 150 or so Labour backbenchers signing the anti-privatisation Early Day Motion it seems almost inconceivable that over 100 of them could be bought off with minor concessions. But then what? If Labour wins again with a fresh mandate, the same initiative is likely to be on the table soon after the election. If the Tories win, as the polls predict, then there is likely to be full privatisation with no concessions. In either case, for more than another year Royal Mail and the Post Office will be starved of funds and provided with little if any direction. And eventually it will be part or fully privatised by one side or the other. The service will deteriorate and both management and the union will be in a weaker position. No one wins.

Compass would like to see a new model of ownership for Royal Mail and the Post Office – one that isn't about private profit

This cannot be allowed to happen. If the status quo and part-privatisation produce a stalemate between the government and union and their supporters, another option has to be found, and quickly.

This report has two sections. In the first we examine why privatisation is the wrong answer to the problems Royal Mail and Post Office Counters face; in the second we set out a range of governance, investment and industrial relations reforms that could form the basis of a new model for Royal Mail that avoids privatisation but enables the modernisation of the service in terms of investment and improved industrial relations. Neither the government nor the union should be a roadblock to such reform.

2. Why Privatisation is the Wrong Answer to the Problems Royal Mail and Post Office Counters Face

2.1 The recent history of Royal Mail

To understand the future of Royal Mail and ensure it is modernised in the right way we have to understand something about its past. In some respects it is amazing that Royal Mail and the Post Office are in as good a shape as they are, as Royal Mail has not been well served by its political masters or regulator for a long time. It has been plundered for cash; the market it operates in has been liberalised without the organisation being modernised; private companies have been allowed to cherry pick the most profitable services and piggy back on the infrastructure for the Universal Service Obligation (the USO, which means the whole country get the same service regardless of where they are) and in effect have been subsidised by the public through less-than-cost access charges; and since the early 1990s it has faced the ever-present threat of privatisation. To cap it all, governments took a pensions holiday from 1990 to 2003 resulting in a huge debt Royal Mail has had to service ever since.

During the period 1981 to 1999 Royal Mail was forced to hand over £2.4 billion in profits to the Treasury. This crippling policy was ended under the Labour government. Yet the Labour government has been too slow to recognise the need for new investment and technologies in Royal Mail. Hence the government did not dispute the price controls set by the regulator in 2001, which maintained some tariffs below the rate of inflation. This means the service offers the lowest price in Europe but funds for modernisation have been severely limited.

Some investment has been provided, such as the government agreement in 2006/7 to an investment loan of £1.2 billion. Yet management has been extremely slow in deploying this, with only half of it having been spent by 2009. There is little evidence yet of new machinery or technology as a consequence of the claimed expenditure of £600 million and even fewer ideas about how and where the balance of £600 million is to be spent.

As an alternative to direct investment, the government has supported liberalisation of the industry, introduced by the regulator Postcomm. This liberalisation has resulted in Royal Mail still delivering 99.8% of previously reserved mail. This is no surprise; no other firm is willing to invest the huge amount of capital required to deliver to 28.4 million addresses. So the competitors have concentrated on winning the profitable bulk 'access' work. This is the

conveyance of mail from firms posting large numbers of letters. But these bulk mailings are collected and driven to Royal Mail sorting offices. Once there, Royal Mail completes the sorting process and delivers the mail, although the envelope is branded with the name of a competitor.

The regulator has so manipulated the terms of these contracts that Royal Mail is forced to pass on efficiency savings to competitors. This allows the competitors to reduce prices below those of Royal Mail even further. As a result Royal Mail has not won a contested contract on 'access'. The competitors have secured 40% of this work. So Royal Mail, a publicly owned and run body, is starved of investment funds because of the liberalisation desires of the regulator who is employed to secure the best deal for the public. Even the Hooper Report recommended that this should be examined. A conservative estimate suggests that bending the market against Royal Mail in this way costs the organisation around £100 million per year.³ It shouldn't be too much to ask that Royal Mail is allowed to operate on normal commercial terms.

In 1994 the Tories tried to privatise the whole of Royal Mail. The plan was defeated because of a backbench rebellion and widespread opposition throughout the country. New Labour has since been looking for the opportunity to part-privatise the organisation. So for 15 years Royal Mail has been in limbo. The regulator has applied the toughest price controls while pushing liberalisation as far as possible. Royal Mail has been opened up to competition with one hand tied behind its back. The management has been waiting for decisive political leadership, and the modernisation process and new technology have not been implemented. The workforce and the union feel they have been fighting a rearguard action to keep the service public.

Of course, the internet has had an impact on our use of mail. This though is a process complementary to the mail service. If individuals are sending fewer letters, then they are also using mail as a delivery route from the internet. We send fewer letters but get a lot more parcels. Businesses have a wider choice of platforms, yet mail remains trusted, effective and capable of supporting multi-media campaigns. This is one reason why, despite the lack of care and attention, the profits of Royal Mail have remained healthy.

2.2 The problem with Hooper

In 2007 the government commissioned Richard Hooper to look strategically at the industry. His report 'Modernise or Decline', as the title suggests, poses a stark choice for the service. But the reality is not whether to modernise – but how to modernise?

With the help of business consultants and academics Compass published a report analysing Hooper's work. In the document 'Case Not Made' Compass showed that the Hooper Report is merely a collection of assumptions and assertions based on little if any factual evidence. Royal Mail is simply not the failed and failing organisation portrayed in the Hooper Report. Furthermore, the European comparators Hooper uses, most notably Germany and the Netherlands, are not the shining examples of efficiency he claims. Germany is profitable because it charges its customers more, not because it is efficient. The Dutch system derives its 'efficiency' on the basis of an operation in a small flat country. Hooper does not compare like with like. Our Royal Mail service is not only the lowest priced service in the EU but also still profitable across all its areas of operation.

From these shaky 'empirical' grounds Hooper concludes that the problems of modernisation and investment, the industrial relations record and the pension deficit can only be addressed together through part-privatisation of the service. With few figures and highly dubious assumptions, Hooper jumps to the ideological position that only privatisation will do. No other options are mentioned or discussed. There is not even any mention of the People's Bank,⁴ which the government now appears to be much more interested in.

Hooper also fails to deal with the issue of timing of any sale: why sell now when it's the bottom of the market? Using data on Royal Mail and its European equivalents, Compass has calculated that the Treasury would receive £900 million less if it conducted a sale now compared with just a year ago. As things stand, within eight years a buyer would have covered their investment; if the pension deficit is dealt with, access charges made fairer and efficiency gains made, the annual profits of Royal Mail could easily meet the private sector investment needed to buy 49% of the business in less than three years. Why give it away so cheaply? Even if you think it makes sense to sell, it makes no sense to sell now.

So we share some of the analysis of Hooper about the problems that need to be rectified, but the case for privatisation is not made. Furthermore, in supposedly looking at all aspects of the service, there is no analysis of the potential disadvantages of part-privatisation. These are considerable.

Our Royal Mail service is not only the lowest priced service in the EU but also still profitable across all its areas of operation

Royal Mail is a natural monopoly in the sense that there is no point in duplicating the infrastructure for the USO. We don't need another set of pillar boxes, a system of door-to-door deliveries and a counters network. Indeed there are huge efficiencies gained from an integrated postal system. Hooper fails to examine any of them. Indeed he fails to look at the inevitable increased transactional costs of breaking up the mail from counters and the money that would go to lawyers and accountants for the contractualised relationship they would ensure – as the broken up parts of the service try to cut costs against each other.

Royal Mail needs to be viewed as what it is: a complex organic entity in which counters and mail delivery work seamlessly together. Rip that apart and inefficiencies would soon bubble up and the public would get a worse service. Just think about the experience of BT. Now that the physical phone lines have been separated from the customer service, dealing with the company on issues like broadband is a nightmare. Consumers fall between two stools, with neither side taking responsibility. It can take weeks or months to move a connection from one house to another. The post will end up like this. Who will have lost your letter – the partly privatised Royal Mail or the separated and still wholly public counter service you gave it to? And prices are certain to increase. The shareholders of the newly part-privatised service will demand it. It's little wonder that TNT, the Dutch operator, delivers 100 gram first-class letters at nearly three times the price of Royal Mail. TNT delivers 50 gram letters at twice the price. Furthermore, TNT has a government-protected monopoly on the delivery of letters at 50 grams or less.

We also assume that shareholder sovereignty would lead to a reduction in non-profitable services with, potentially, a big impact on rural areas and domestic customers. A new management with a large strategic stake in the service will direct it for their purposes. Why else would they invest if there was no return? Indeed it would soon stop being a service and become a business. More and more profitable parts would inevitably be hived off.

Not only does the Hooper Report fail to make the instrumental case for privatisation, it ignores totally the intrinsic case for a publicly accountable service. This is the recognition that there is more to some public services than what they cost and what they make.


One of the wonderful things about the postal service is that everyone who comes into contact with it is treated equally. It doesn't matter how big your front door is or how long the path to it – you get the same service. When we stand in the queues at the post office we are all equal – regardless of the size of our wallets or purse. All citizens receive the same service, whether they live in a large city or a small rural community. Whilst

processing huge mailings from businesses, Royal Mail also prioritises services for blind customers. The pursuit of profit puts all this in jeopardy. The erosion of the public service ethos to make way for private sector profit will only serve to undermine social cohesion still further, as privileged services will be developed for wealthier users, leaving only a minimal one for the majority.

Having said all this, Compass recognises that there are three central problems that have to be addressed:

1. The pension deficit
2. The need for further investment and commercial freedom
3. The industrial relations problem.

How can these problems be solved without resorting to the old and tired politics of privatisation?



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3. Commercial Freedom: Not for Profit but for the People

Before we attempt to answer the challenges of the Hooper Report, it is worth quickly setting out the kind of service we want to achieve. We have a vision of a dynamic and innovative public service – one which is ‘customer friendly’ but that continues to treat us as equal citizens.

In Royal Mail of the near future the workforce must be active participants in the continual and everyday modernisation necessary to ensure the service is the best possible. Indeed, because of their intimate knowledge and commitment to the service they will be viewed as key stakeholders in a new Royal Mail. For us it is not the one-off big bang of a new governance structure, important as that is, that will transform the service, but the everyday constant reforms that only an active, engaged and trusted workforce can provide.⁵ Important elements of the delivery process can be automated but it will remain a people-centred business. This is why privatisation will not work – because it will make the workforce more hostile to reforms; only building consent will get them on board.

There is a tremendously warm public attitude towards Royal Mail. This will be lost under part-privatisation. No one loves London Electricity; few even know who owns it. A service run for profit can't be a national icon and can't serve as part of the social fabric of the nation. It certainly can't help reinforce our sense of national identity.

But the inspiration needs to be practical too. Some other national systems are delivering services with new technologies that are not yet being used by Royal Mail. There is, for example, ‘hybrid mail’, where customers provide data which the service provider then downloads, prints, envelopes and delivers. There is also ‘intelligent mail’, where bulk mailings can be tracked and traced individually from collection to delivery. Royal Mail needs to acquire this capacity. At the same time there are new services linked to internet trading being offered by some providers. For example, La Poste (France) is offering home collections. A new generation of walk sequencing machines is also necessary – these automatically sort letters to delivery codes, removing manual sorting. As Hooper notes, comparable EU operators are using these machines to cover 85% of letters handled; Royal Mail doesn't use them at all. Same day deliveries in urban areas could transform the use of the system. The mixture of more services and increased use of technology means job losses could be kept to a minimum.

Just a little imagination is required to develop the huge potential in Royal Mail. We support the call for a People's Bank to be offered through the Post Office branch network. The government's decision to award the Post Office Card Account to Royal Mail is an important commitment to the Post Office network, which follows years of stripping provision by the Post Office of vital services and payments, such as TV licences and car licences. But without supplementary services offered through the network, closures will continue. Only by fully developing banking and micro-credit services through the Post Office can the network be brought to profitability. At the same time, a People's Bank can offer a crucial lever against financial exclusion. The network of around 12,000 Post Office branches can reach much larger numbers than any other financial institutions. In line with the government's commitment to micro savings via the Savings Gateway Bill, we would like to see it making a commitment to micro credits as a tool for reducing poverty. Such developments can drive out the loan sharks from the poorer communities, which are preying on vulnerable individuals.

If this is the kind of service the nation needs, how do we get there? Here we need to respond to the three central problems identified in the Hooper Report but answer them without resorting to the tired and now discredited response of privatisation against the wishes of the public and the workforce. In short how do we get modernisation with consent?

3.1 The pension deficit

In one sense this is the easiest issue to deal with. The Hooper Report recognises that the government must accept responsibility for the pension deficit. We agree. So, generously, does the government. The deficit is the result of an extended holiday in pension contributions by the employer, the government, over a period of 13 years. This ran up a deficit of around £3 billion by 2006 and is estimated to have doubled since. It costs Royal Mail around £280 million a year to service. Elementary justice demands that postal workers have their pensions (their deferred earnings), which were negotiated and agreed by their employer, made secure for the future.

We know the government is worried about looking as if they are favouring public sector workers at a time

In times of uncertainty and anxiety like these, the government should lead by example and take responsibility to deliver the pensions deal it negotiated and agreed to

when employees in the private sector are seeing their pensions cut. But working in the public sector is in part a trade-off between high salaries and better terms and conditions – like a secure pension. In times of uncertainty and anxiety like these, the government should lead by example and take responsibility to deliver the pensions deal it negotiated and agreed to. The government must not renege on it but instead become an exemplar of best practice, providing security and building trust. Having said that, there can be no easy ride for the workforce. In return for the full funding of the pension the challenge of modernisation is one they must help face.

The removal of the pension deficit will provide Royal Mail with around £280 million additional capital per year, for the next 15 years. In a single stroke the finances of Royal Mail are transformed – whether the company is privatised or remains in the public sector. Yet nothing could alienate public opinion further than to see the government nationalising the debt of pensions whilst allowing the privatisation of profit. This is what the public has seen happen in the banks these past months, and it has made them very angry. The government now needs to commit to putting the pension deficit right but without part-privatisation. But the confidence to do this will require a new governance structure for Royal Mail and a fresh start for the service.

3.2 The need for investment and commercial freedom; a new model for Royal Mail

Once the pension deficit is dealt with, as the government, Hooper and the union say it must be, then a host of governance options are opened up for a new Royal Mail. Let's remind ourselves here that the status quo is unlikely to be an option. Any future government is likely to attempt at least part if not wholesale privatisation of the service. A new model is needed. The key principles behind such a new model should be that:

- It is wholly publicly accountable; with accountability extended and deepened beyond parliament.
- All profit and surpluses are to be locked into the service and re-invested.
- Additional funding is made available from outside government finance as well as funding from efficiency gains.
- There is an opportunity to bring in fresh management – with private sector experience where necessary and appropriate.

Fortunately New Labour has ensured that a number of hybrid models, which meet these requirements, are already on offer. Two of them, Network Rail and Welsh Water, were actually

set up by this government, and the third, the BBC, has been modernised by them. This doesn't mean there is an off-the-shelf, ready-made alternative for Royal Mail. But we can learn from the experience of these three models and apply the most appropriate elements to a new modernised Royal Mail.

3.2.1 Network Rail

In many respects Network Rail provides the most interesting model for a new Royal Mail, not least because it was created as a result of a failed privatisation. In the collapse of Railtrack and its rebirth as Network Rail we can see a possible future for Royal Mail – one where the separation of the service, counters from postal delivery, mirrors the disastrous separation of track and wheel on the railways. After a number of rail accidents confidence in the still relatively new Railtrack diminished quickly. The company had lost its ability to manage the rail network and the government stepped in, effectively renationalising the service.

With a bit of imagination we should be able to miss out the failed privatisation stage for Royal Mail and jump straight to a long-term solution that works.

Network Rail's status in terms of governance is defined as a not-for-dividend company. Like Royal Mail it operates a large infrastructure that needs constant modernisation. For track, signalling and stations, we can as easily read pillar boxes, vans, sorting offices and post offices. Network Rail has a monopoly of the rail network, including the track, signalling, bridges, tunnels and stations, just as Royal Mail monopolises much of the sorting and delivery service.

Network Rail operates under a network licence that contains a set of conditions under which it must operate such as ensuring that the infrastructure is safe and able to meet the requirements of the train operators. Currently Network Rail has a board of 14 directors, 6 executives and 8 non-execs. The Network Rail chairman is Sir Ian McAllister and the chief executive Iain Coucher, both recruited from the private sector and both have a reputation for getting things done.

Network Rail is set objectives by the Office of Rail Regulation. The network operator is required to demonstrate in its annual business plan how it proposes to operate, maintain, renew, replace, enhance and develop the network. It must manage the quality and capability of the network in accordance with best practice, in a timely, economic and efficient manner so as to satisfy the reasonable requirements of its customers and funders.

The company's key purpose is to provide the public with a service rather than to maximise profits for shareholders. Profits generated are reinvested into its core function – the maintenance, renewal and development of the UK's rail network.

Network Rail is a membership organisation with 118 members drawn from the railway industry and the general public. Companies that operate trains on Network Rail track currently have the right to nominate industry members and many do. The role of a member of Network Rail is intended to be equivalent to that of a shareholder in a publicly listed company. Public members are drawn from a cross-section of the public. Just like Royal Mail, it is regulated by an independent regulator, the Office of Rail Regulation, while receiving part of its funding direct from government.

Network Rail's funding has two main components: direct funding from the government and access charges paid through the franchised train operators. The company also receives rental income from its property and payments from freight and open access operators. The money available from government is set by ministers (in a Statement of Funds Available), which determines the amount of work that can be carried out on the network and the level of service offered to operators through an iterative process involving the regulator. This is a quinquennial process setting out the work programme in five-year control periods. However, in addition to this funding Network Rail can borrow privately. Network Rail's financing requirements are principally met by debt raised from the capital markets. In total the company has borrowed close to £20 billion, which does not count as government borrowing because technically it is deemed by the Office for National Statistics not to be in the public sector. However, the borrowing is essentially guaranteed by government, which means that it is cheaper. Network Rail is keen to try to obtain money that is not guaranteed by the state but this may not now be possible given the current difficulties in the capital markets.

This suggests the basis of a similar model for Royal Mail although there is one aspect which would need to be improved on – its governance structure. With over 100 members and a structure that does not offer them sufficient power, the stakeholders of Network Rail face an uphill struggle to establish a strong and coherent voice. As a result, the directors of Network Rail have been allowed too much leeway and have not been sufficiently called to account. Currently, this issue is under examination and there have been a number of suggestions for strengthening the role of the members.

This point aside, Network Rail offers many of the features we would want to see in a new Royal Mail; it is operationally free from government; it offers the efficiency of a united and holistic infrastructure; it has strong private sector management; and it can borrow on

the open market without affecting the government's debt. It is a New Labour success story that could in large part be applied to Royal Mail.

Christian Wolmar, the author of several books on the railways including a critique of rail privatisation, *On The Wrong Line*, said:

Railtrack could never succeed because it was an infrastructure company in need of long term investment decisions that was beholden to the short term interests of its shareholders. The Network Rail model is far more effective, as has been shown by a continued improvement in performance since it was created six years ago. This model is clearly suitable for a public service such as the Post Office provided that adequate governance procedures are built in to the structure. It is infinitely preferable than part privatization because that would inevitably lead to narrow commercial interests determining priorities.

Network Rail offers many of the features we would want to see in a new Royal Mail

3.2.2 The BBC

To find a solution to the governance issue we can turn, like we do many nights of the week, to the BBC. The BBC's legal status is established by a Royal Charter, renewable every ten years. Each Charter is accompanied by an agreement between the government and the Corporation. The Charter and Agreement oblige the BBC to produce and transmit a range of quality programmes that seek to inform, educate and entertain.

In 2007, the government introduced a new BBC Trust to replace the old Board of Governors. The purpose of the old Board was, in effect, to protect the BBC primarily from political interference. The prime responsibility of the new Trust is to make the BBC's accountability to the licence fee payer explicit. The trustees are responsible for ensuring 'public value'. The Trust is appointed by ministers based on a rigorous selection process overseen by the Commissioner for Public Appointments.

The Charter establishes the role of the Trust and in particular its relationship to the Board. The Trust:

- Is the guardian of the licence fee revenue and the public interest
- Acts separately from the Executive Board and must maintain its independence of the Executive Board

- Has the function of assessing the performance of the Executive Board in delivering the BBC's services and activities and holding the Executive Board to account for its performance
- Must represent the interests of licence fee payers and exercise rigorous stewardship of public money
- Must ensure that arrangements for the collection of the licence fee are efficient, appropriate and proportionate
- Must have regard to the competitive impact of the BBC's activities on the wider market and adopt a fair trading policy and hold the Executive Board to account for compliance with it
- Must keep under review the financial needs of the BBC for the purpose of ensuring that the Executive Board is not authorised to spend more public money than is needed for the appropriate discharge of the Board's functions
- Must examine the value for money achieved by the BBC in using the sums paid to it
- Must regularly discuss with the Comptroller and Auditor General the possible scope of its audit programme and which individual reviews within that programme would be particularly suited to the National Audit Office.

This new model was hailed by the then Secretary of State for Culture, Media and Sport, Tessa Jowell MP, when it was introduced. She said, 'The BBC Trust may well, in time, prove a model for accountable governance and regulation in public bodies.'⁶

Finally, the BBC is an interesting hybrid model for Royal Mail as it is allowed both to set up joint ventures with private sector partners and to borrow money outside the Treasury – the current limit being set at £225 million.

What is impressive about the BBC model is that it continues to embody public sector values but within a red hot commercial world; in part this is because it embraced new technology, in particular the internet, and has led the broadcasting world in many respects.

Its secure status as a public sector body enabled it to do this. If modernisation in the public sector can be achieved by the BBC, then it can be achieved by Royal Mail.

But a revitalised Royal Mail could go further. Instead of accountability just residing at national trust level, Royal Mail and in particular Post Office Counters could become more

What is impressive about the BBC model is that it continues to embody public sector values but within a red hot commercial world

locally and regionally accountable through a requirement to share the forward planning of services with the Scottish Parliament, the Welsh and Northern Ireland Assemblies, the Greater London Authority and the county councils. They would be able to ask questions and call for a community impact report on service changes and branch closures. In this way the service could be brought closer to the people it is there to serve.

3.2.3 Welsh Water

Welsh Water is one other interesting potential alternative model for Royal Mail. It too is a not-for-profit company with a membership. It is a water and sewerage company that serves 3 million people in Wales and bordering regions of England, employs 165 people directly and a further 3,000 staff through specialist contract partners. It has an annual turnover of circa £550 million. It was created out of failed private ownership, is regulated by Ofwat and operates under a unique not-for-profit business model whereby all financial surpluses are reinvested for the benefit of its customers.

Welsh Water exists to provide an efficient and sustainable service in the best interests of its customers. Its vision, or 'banner' as the company refers to it, is 'to be recognised by our customers as the best water company in the UK'. To achieve this, Welsh Water has committed to:

- Achieve significantly lower bills than would any other company
- Continue to be upper quartile in industry league tables of service performance
- Deliver successful long-term asset management in the best interests of future customers and the environment.

Welsh Water is a private single-purpose company with no shareholders. Reducing financing costs and delivering its annual 'customer dividend', which reduces customers' bills, are central elements of the business strategy of Welsh Water. Since 2001, the company has returned £98 million as 'customer dividends'. Over the same period it has reduced the amount to which the company is leveraged from the original 91% of borrowing to below 75%, close to its 70% target. The cost of borrowing has dropped dramatically for Welsh Water, in part because the equity markets like the security of an investment vehicle that is stable and not subject to takeover.

In describing the business model, Richard Curtis, Company Secretary of Welsh Water, says it has given the company 'new legitimacy with our key stakeholders which in today's regulatory environment is beneficial for the business, our customers and the environment'.

All three organisations were either successfully created by the government, in the case of Network Rail and Welsh Water, or were reformed to make them more accountable to the public, in the case of the BBC. Between them they present the prospect for a new Royal Mail that:

- Is run solely for public benefit and not for profit
- Allows for flexibility in borrowing outside Treasury constraints
- Permits access to private business expertise
- Increases accountability.

But there is one final issue Hooper raises that has to be addressed.

3.3 Building the best industrial relations partnership

We know that this is a prime concern of the government. But past history shows that the management and the union are quite capable of negotiating the substantial changes that the new generation of technology brings. Major agreements covering technology were secured with the union in the 1970s through the Letter Post Plan, in the 1980s with the Revised Revision Procedure, in the 1990s with the Way Forward Agreement, and in 2007 with the Pay and Modernisation Agreement. The union now says it is prepared to make a further modernisation agreement to cover the next generation of machines, and the rationalisation of the mail centres and delivery offices.

But the relationship between the management and the workforce in Royal Mail could still be improved and needs to be if the challenges of modernisation are to be met. It is clear from his comments and his report that Hooper sees the workforce and its union, the CWU, as a barrier to modernisation. The government, it seems, holds a similar view.

We can play the blame game too, but this doesn't get us very far. It takes two sides to create a relationship problem. The union may well have behaved defensively but then it has the perception that it faces a hostile political and regulatory regime – with some justification. Sorting offices still have the feel of Victorian mills to them – where workers are regimented and controlled rather than given freedom to do the job as they know best. From the postal workers we have spoken to there is a huge amount of pride in a job well done, serving their community. They feel embattled and defensive. The management refuses to share any of their business plans with the union. This is no way to run a modern organisation, which will always be based on the commitment and dedication of its staff. But what matters now is how relations could be improved to ensure the service is as efficient and responsive as possible.

In what will always be a labour-intensive service, the workforce should be part of the solution and not seen as part of the problem. Ultimately it will be the responsibility of the

management and government to create a climate in which the workforce feels properly engaged. But the workforce and its union need to respond positively, too – taking more responsibility not just for terms and conditions but for the modernisation and reform programme. The service will become much more efficient when the workforce can focus on the customer and not be looking over their shoulders, worrying about liberalisation, privatisation or the hole in their pension fund.

So ending the decade and half long threat of privatisation would transform in an instant the industrial relations frictions. The establishments of a new governance structure, like the ones suggested above, would allow a fresh start and the settlement over the pension deficit would reassure the workforce that their employers deliver on their promises. But more can and must be done. Once again the government has already engineered successful models, which could be applied to Royal Mail and the Post Office.

3.3.1 Agenda for Change in the NHS

Agreed in 2004, Agenda for Change was the most radical shake up of the NHS pay system since the NHS began in 1948. It covers more than 1 million people and harmonises their pay scales and career progression arrangements across traditionally separate pay groups. All the health unions were involved along with the four UK health departments and the NHS Confederation representing all the NHS employers. The new pay system provides benefits for individual staff and NHS employers. The system provides employers with greater flexibility to:

- Devise new ways of working that best deliver the range and quality of services required, to best meet the needs of patients
- Design jobs around the needs of patients rather than around grading definitions
- Define the core skills and knowledge they want staff to develop in each job
- Pay extra to address local recruitment and retention difficulties.

For staff the key benefits include:

- A system that that is fair and transparent
- Recognition and reward for the skills and competencies staff acquire throughout their career
- Harmonised conditions of service.

It is an excellent example of government-led progressive industrial relations. As a one-off measure it has delivered lasting change in this crucial institution built on consensus and


partnership and has served the NHS well. It could be applied successfully to the modernisation of industrial relations practices in Royal Mail.

3.3.2 The Education Workforce Agreement

The second example provides a process of ongoing reform; the Workforce Agreement and Monitoring Group is the social partnership vehicle in education for the 11 organisations representing employers, the English and Welsh governments and the school workforce unions (with the exception of the NUT). It came together in 2003 because of the challenge of recruiting and retaining teaching staff, maintaining morale, and associated issues of terms and conditions – especially hours.

Progress has since been made on the basis of a consensus about what is best for the system and the children it is there to support. It has created a national agreement that is statutory and enshrined in the School Teachers Pay and Conditions Document. Successful reforms to date include a review of whole school staffing structures, new systems for teachers' performance and management, changes to teachers' pay structures and new professional standards. Local social partnerships have a crucial role to play by offering support and challenges to the implementation of the reforms that are sensitive to the local situation. It has resulted in better terms and conditions for staff and improved educational outcomes. There is a united front on key issues with union members agreeing to work in partnership to promote workforce modernisation and reform. Best practice is shared clearly and consistently.

In both education and health the government has created new partnership forums that have built consent which has led to service improvement for the public. If it can be achieved in these two sectors then it can be achieved in Royal Mail.

A black and white photograph showing a hand inserting a white envelope into a dark mailbox slot. The mailbox is made of a textured material, possibly metal or heavy plastic. The hand is positioned at the bottom left, with the index finger and thumb holding the envelope. The envelope is partially inside the slot, with its top flap visible. The background is dark and out of focus.

Royal Mail needs a fresh start to build on its strengths as a great public body – not a continuation of old conflicts in an unpopular privatised form.

7. Conclusion

The success of any government is largely measured by the institutions they leave behind. Think about the Attlee government of 1945 and the NHS; the Wilson government of the 1960s and the creation of the Open University; Thatcher and the privatised utilities of the 1980s; and the Blair government setting up the parliament in Edinburgh and the Assembly in Wales. What will be the institutional legacy of the Brown government? If it gets it right, and if the union and the Parliamentary Labour Party can agree, it could be a new Royal Mail, one modernised by consent. If the right model is adopted, combining the best elements of the features identified in this report, then it would be the kind of popular and accountable model the Conservatives, if they were to win the next election, would fear tampering with.

Such a model, based on a mix of Network Rail and the BBC, would be a brave and bold step. But if it is taken it could help provide a winning platform for the government for the next election. It would demonstrate imagination and show that the government is willing to listen to the public. It would heal wounds and suspicions within the Labour Party.

None of this will be easy. But the alternatives of defeat at the hands of the Labour backbenchers or privatisation but only with Conservatives' help are both too awful to contemplate. The former would lead to years of drift, the latter would saddle us with a privatisation that, like rail, the country soon regrets. In both cases the public will lose out.

Privatisation is not the future, it is the past. The Danish government has bought back its 22% stake in Post Danmark, which it sold to private equity firm CVC, and the French government has put on hold its plans to privatise La Poste. The future for Royal Mail is modernisation by consent. The Bill that is currently just starting its parliamentary process could easily be amended to set up a new Royal Mail along the lines suggested here. It would just take both sides to step back from the brink and put the interests of the public and the service first. Royal Mail needs a fresh start to build on its strengths as a great public body – not a continuation of old conflicts in an unpopular privatised form.

If the government and the union can take the kind of path outlined in this report then both sides would prove that they have not run out of steam – far from it. Instead, a new chapter will have been opened in the history of a much loved and much needed British institution – not through conflict but through consent.

Endnotes

- 1 Hooper et al (2008) *Modernise or Decline*, <http://www.berr.gov.uk/files/file49389.pdf>
- 2 See: <http://clients.squareeye.com/uploads/compass/documents/compass%20hooper.pdf>
- 3 Access charge loss to Royal Mail based on first half-year figures from Royal Mail for 2008/9 of 2.5 billion items making a projection of 5 billion items for the year multiplied by the 2p loss per item, which is a Royal Mail management figure that equates to an effective subsidy to the private sector of £100 million per year. This should be renegotiated to create a level commercial playing field.
- 4 See: http://www.neweconomics.org/gen/z_sys_publicationdetail.aspx?pid=284
- 5 See: <http://clients.squareeye.com/uploads/compass/documents/CO-PRODUCTION.pdf>

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About Compass

Compass is the democratic left pressure group whose goal is both to debate and develop the ideas for a more equal and democratic society, then campaign and organise to help ensure they become reality. We organise regular events and conferences that provide real space to discuss policy, we produce thought-provoking pamphlets, and we encourage debate through online discussions on our website. We campaign, take positions and lead the debate on key issues facing the democratic left. We're developing a coherent and strong voice for those that believe in greater equality and democracy as the means to achieve radical social change.

We are:

- An umbrella grouping of the progressive left whose sum is greater than its parts.
- A strategic political voice – unlike thinktanks and single-issue pressure groups Compass can develop a politically coherent position based on the values of equality and democracy.
- An organising force – Compass recognises that ideas need to be organised for, and will seek to recruit, mobilise and encourage to be active a membership across the UK to work in pursuit of greater equality and democracy.
- A pressure group focused on changing Labour – but Compass recognises that energy and ideas can come from outside the party, not least from the 200,000 who have left since 1997.
- The central belief of Compass is that things will only change when people believe they can and must make a difference themselves. In the words of Gandhi, 'Be the change you wish to see in the world'.

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