



National Audit Office

Improving the efficiency of postal services procurement in the public sector

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Improving the efficiency of postal services procurement in the public sector:
Case Studies, HC 946-II, Session 2005-2006

Improving the efficiency of postal services procurement in the public sector:
A good practice guide, HC 946-III, Session 2005-2006

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EXECUTIVE SUMMARY



1 All public sector organisations rely to varying degrees on the collection, transport, and delivery of letters and parcels (postal services) in their communications with citizens, internally, and with other public sector bodies. Of the £750 million spent annually by the public sector on courier and postal services, nearly £650 million (representing 10 per cent¹ of the total UK mail market) is spent on post, with £100m spent on couriers. Some £250 million is spent by central government departments on post, with the two biggest spenders, the Department for Work and Pensions and HM Revenue and Customs, accounting for over half and the top ten organisations accounting for 95 per cent of the total.

2 The significance of postal services does not lie in costs alone. In many parts of the public sector the use of postal services is vital to the successful delivery of key public services, for example to deliver information, benefit payments, or application forms. Despite the growth in e-services, postal services remain, and will do for the foreseeable future, an essential part of departments' and agencies' interactions with citizens.

3 Historically Royal Mail has been the monopoly provider of letters under 350 grams as well as being the Universal Service Provider in the UK.² However, since the Postal Services Act 2000, the mail market has been increasingly opened to other suppliers. Liberalisation has occurred in two phases. Phase One was implemented in 2003, when for the first time, customers could use alternative suppliers to Royal Mail for bulk delivery of letters weighing less than 100 grams or costing less than

80p. Phase Two, in January 2006, removed the final restrictions; in effect no part of the postal market is now reserved for Royal Mail alone, subject to an alternative operator having a licence from Postcomm, where this is appropriate. In mid 2005 Royal Mail was still the dominant supplier having over 97 per cent by volume of total market share across the public and private sectors.³

4 The focus of this report is on how public sector organisations can become more effective procurers of postal services, making the appropriate product and supplier choices and reducing their costs. In particular, we assessed:

- a** the progress of public sector organisations in achieving efficiency in their procurement and management of postal services; and
- b** what more needs to be done by public sector organisations and the Office of Government Commerce to improve performance and realise financial and quality of service benefits from their postal services, supported by examples of good practice from organisations in both the public and private sectors.

In identifying opportunities for efficiency gains and reduced costs, the service received by the customer has always been at the forefront of our thinking. The approaches to improved efficiency we highlight in this report and the accompanying volumes, therefore also include the effects on the quality of service provided to customers.

¹ Royal Mail, 2004-05.

² The Universal Service Provider (USP) defined under The Postal Services Act (2000) as the company responsible for delivery of mail to each address, and the collection of mail from every access point, in the UK at least once every working day.

³ Postcomm 2005 Competitive Market Review (based on figures collected for quarter two, 2005-06).

Key Findings

5 On the current performance in the use of postal services across the public sector. We found that there is a wide range of performance across the public sector.

The average cost per mail item varies from 31.1p to 21.5p.

Proportion of outbound mail achieving volume discounts varies from 93 to 15 per cent.

Departments or agencies with highly centralised output, in particular the Driver and Vehicle Licensing Agency and National Savings and Investments, are able to achieve high levels of volume discounts for their mail, at a level that compares well with leaders in the private sector. The Department for Work and Pensions has a relatively high cost per item which largely reflects its highly distributed network of offices and use of first class mail to send out benefit payments to meet its requirements for security, timeliness and certainty of delivery date. It has, however, made progress in this area. For example, by issuing Winter Fuel payments for 2005 using a second class 'work share'⁴ product rather than first class standard tariff, the Department saved over 10 pence per item (which it estimates will generate an annual saving of some £1.2 million) with no adverse impact on customer service. In general, postal services procurement has been reviewed by the bigger-spending departments, but it has been a low priority area for the majority of organisations.

6 On the potential financial savings that can be achieved across the public sector. Our four public sector case study organisations (the Department for Work and Pensions, HM Revenue and Customs, the Driver and Vehicle Licensing Agency, and National Savings and Investments) could demonstrate that they have in recent years achieved significant improvements in the efficiency with which they procure postal services.

7 Despite the progress already achieved, we estimate that additional annual savings of nearly £10 million are achievable across the entire public sector by 2006-07, gradually rising to £31 million by 2008-09, from improved efficiency in four main areas:

- a **Increased use of price discounted 'work share' products:** we estimate that across the public sector, annual savings of £9 million are possible by 2008-09.
- b **Increased use of lower cost second class and products with longer delivery timescales:** we estimate that savings of £9 million are possible across the public sector each year from 2008-09 by organisations appropriately revising the mix of mail classes they use.
- c **Increased use of competitive tendering leading to lower cost products for the same or improved levels of performance:** We estimate, based on evidence from customers, that organisations can save, on average, 10 per cent on postage costs⁵ by using alternative suppliers for 'Downstream Access'⁶ or 'end-to-end'⁷ delivery (based on 2005 pricing structures). This could potentially save £8.5 million across the public sector annually from 2008-09.
- d **Reductions in the volume of 'undeliverable' mail:** Reductions will generate productive time savings for processing mail and postage procurement savings, resulting in estimated annual savings of some £4.5 million across the public sector by 2008-09.

We reviewed the feasibility of the scale of potential benefits with our case study organisations and have used these figures to estimate savings across the wider public sector, including the education⁸, health and local government sectors⁹ (**Figure 1**). These potential savings may be used as benchmarks against which performance improvement can be judged. Many of the improvements we have identified can be done at low cost and within short timescales, in particular: changes in class of mail, increased use of competitive tendering, reduction in volume of undeliverable items through data cleansing routines, and better choice of mail products (such as Cleanmail and Packet Post¹⁰). The accompanying 'Good Practice' guide to this report provides examples of organisations in both the public and private sectors that have realised efficiency gains in their postal services through these and other approaches.

4 Postal 'worksharing' involves mailers performing activities such as preparing or sorting mail, often by geographic areas, before providing the mail to their suppliers for final sorting and delivery. They obtain a discounted price as a result, depending on the volumes involved.

5 Savings levels can vary, with some customers achieving significantly higher discounts.

6 Downstream access is where postal services companies other than Royal Mail collect mail from a single customer or from multiple customers (a process referred to as 'consolidation'), before injecting the mail into Royal Mail's supply chain for final delivery.

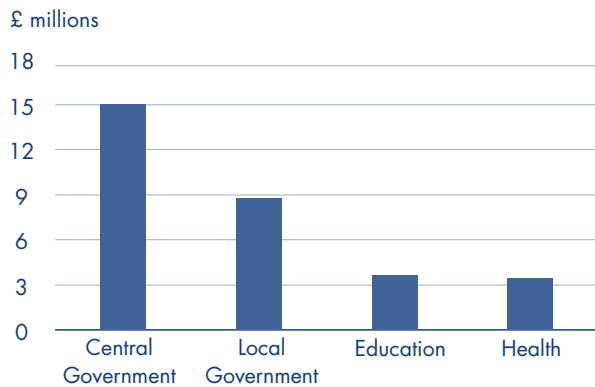
7 End to end service suppliers provide a full service from collection point to delivery destination (in other words mirroring the service provided by Royal Mail).

8 The education sector referred to in this report consists of further and higher education institutions in England, Scotland, Wales, and Northern Ireland.

9 The health and local government sectors referred to in this report cover England, Scotland, Wales, and Northern Ireland.

10 Cleanmail is a Royal Mail product offering discounts based on basic address presentation requirements. Packet Post, a Royal Mail product, offers discounts on weightier items based on minimum yearly volumes.

1 Total potential annual savings across the public sector in 2008-09



Source: National Audit Office

NOTE

Local Government, Health, and Education sectors cover England, Wales, Scotland, and Northern Ireland.

8 On the extent to which centrally led initiatives could contribute to improved performance. In the light of market liberalisation, OGCBuying.solutions¹¹ will be establishing mail service framework agreements with a number of suppliers for use by all public sector organisations. A key feature of these frameworks has been the close involvement of the main central government clients in their design and negotiation, resulting in advance commitments on the part of departments to use the frameworks. This is an example of good practice that could be used to good effect on future frameworks for other services and commodities. As a result OGCBuying.solutions anticipates that 60 per cent of total public sector mail spend will go through the frameworks. The agency estimates that use of the frameworks has the potential to generate savings of £30 million a year from 2007-08 onwards through lower prices (9 to 30 per cent savings on particular products) as well as unquantified benefits of reduced tendering and support costs. There is some overlap with the four areas we have identified for savings, particularly ‘increased use of competitive tendering’ (though, of course, use of the frameworks does not necessarily entail switching suppliers). Furthermore, as part of the implementation of the frameworks, OGCBuying.solutions will provide enhanced management information, enabling improved contract and supplier management.

9 On further aspects of the public sector’s approach that inhibit efficiency. In addition to the potential financial savings, we identified three further aspects of the public sector’s use of postal services that adversely affect efficiency and service quality:

- **Post is not always considered as part of an integrated communication strategy.** Few public sector organisations have a clear understanding of the willingness and preference of their customers to use lower cost communication channels such as the internet and telephone. As a consequence they have missed significant opportunities to reduce the demand for post and therefore cost. The scale of these opportunities is well evidenced by the work of the Pension Service of the Department for Work and Pensions which, through a switch to greater use of the telephone to meet its customers’ preferences, estimates that it will reduce the volume of in-bound mail by 60 per cent.
- **Failure to identify and realise the opportunities for joint working.** There is limited evidence of public sector organisations working together to aggregate their mail volumes despite the fact that many will send mail to the same customers often on related aspects of business. For example, HM Revenue and Customs and the Department for Work and Pensions have recognised that an opportunity may exist to rationalise the mail they send to employers but negotiations are at an early stage. There are opportunities for smaller organisations to centralise their mail production or sortation with other similar sized bodies to be able to take advantage of product discounts and economies of scale in equipment and productive time, but there are few examples of this occurring. There is also limited evidence of public sector organisations taking advantage of the more favourable terms other organisations have negotiated with suppliers.
- **Management structures for postal services are often too fragmented.** Responsibility for post is rarely centralised and more often dispersed across the organisation making it very difficult to implement efficiency measures such as aggregating mail to achieve volume discounts. Local managers are rarely held accountable for reducing postal costs, and information on postal spend can be better collated and analysed to enable organisations to take full advantage of the contracts they have negotiated.

¹¹ OGCBuying.solutions is an executive agency of the Office of Government Commerce. Its role is to deliver value for money gains for central civil government and the wider public sector through its dedicated, professional procurement service providing central purchasing contracts and catalogues.

Overall conclusion on value for money

10 Public sector organisations have made good progress in improving the efficiency of their postal services procurement as highlighted by the examples in our four case study organisations and the range of other successful initiatives cited from other public bodies in this report and associated volumes. Our analysis, however, of comparative performance indicates more needs to be done before the public sector is achieving full value for money from its postal services procurement. If our recommendations below are implemented fully then an estimated annual saving of £31 million is achievable by 2008-09.

Recommendations

11 We identified six main aspects of performance in the procurement of postal services for public sector organisations to focus their efforts on improving. These are summarised in **Figure 2 on page 6**. To help organisations to implement these recommendations and realise the potential for financial savings we have highlighted the good practice most likely to achieve better performance in two associated volumes published alongside this report (both associated volumes are also available on our website at www.nao.org.uk):

- A guide to help public bodies improve efficiency, focusing on six areas and drawing on examples of good practice which have enabled organisations in both the public and private sectors to reduce their postage, printing, and processing costs while at least maintaining levels of service delivery.
- A case study volume setting out in more detail the progress, achievements and scope for further improvements in our four case study organisations as well as a ‘good practice’ private sector case study.

From our analysis of public and private sector organisations that have made efficiency improvements, we believe the benefits brought about through the carefully managed implementation of our recommendations will outweigh implementation costs. It is difficult to be precise, however, about these costs because many of the improvements identified are dependent on wider changes in organisational policies, business processes and IT and will differ from organisation to organisation. This emphasises the need for robust business cases for change and close working with suppliers if the recommendations are to be successfully implemented and the potential savings realised.

12 To assist OGCBuying.solutions in helping public sector organisations improve the efficiency of their postal service procurement and secure the best deals, including maximising the benefits achieved from the framework agreements for postal services, we make the following recommendations. OGCBuying.solutions should:

- a **Promote public sector interests in the market place and with the regulator to strike better deals with suppliers and offer a co-ordinated response to the regulator.** Public sector spending represents ten per cent of the total mail market. There has, however, been no single, co-ordinated face to the market to negotiate on behalf of the public sector. OGCBuying.solutions, through framework agreements, can encourage suppliers to, for example, develop more innovative products for secure payments and provide alternative delivery timescales. The regulator, Postcomm, consults customers on a range of important issues including pricing and operational standards of practice. OGCBuying.solutions needs to do more to collect views from across the public sector (if this approach is acceptable to its customers, such as local government, and does not preclude their decision-making abilities) and provide co-ordinated and hence more forceful promotion of these views to the regulator.
- b **Work to ensure that the potential benefits from the postal framework agreements are realised.** OGCBuying.solutions estimates that the public sector can save £30 million per year through use of the frameworks (if the majority of public sector spend goes through the frameworks); however the agency needs to continue to work to minimise the risks involved. The key risks include:
 - Capacity for tendering and implementation of the frameworks at departments, centrally at OGCBuying.solutions, and at suppliers is exceeded by demand. The agency will need to manage the demand for the use of frameworks and manage implementation in a phased manner across the public sector. Furthermore, suppliers’ capacity to provide delivery services in a newly liberalised market will need to be monitored to ensure that service performance remains above minimum service standards.

- Inadequate customer engagement across the wider public sector, particularly local authorities, education, and health could potentially result in low demand and implementation of the frameworks within these sectors. The agency has begun engaging customers, particularly in central government, and recognises more work is required in this area. The main change agents for local government, the Office of the Deputy Prime Minister sponsored Regional Centres of Excellence, are also addressing this specific risk through the engagement of local authorities.
- Good postal services practices that are outside of the main thrust of the frameworks will not be supported and encouraged centrally. The frameworks focus on contract and supplier management. In our view significant savings and increased effectiveness are possible in other good practice areas, such as increased use of 'work share' products and co-ordinated communication strategies. The agency and the Office of Government Commerce (in its role to spread good procurement practice across the public sector) need to work to incorporate these good practice points into their engagement and implementation work with public sector customers. The two bodies should seek to work with other public sector organisations who promote good practice in this area. For example, the Central Office of Information has successfully worked with the public sector to increase postal efficiency, in the areas of customer data management, marketing strategy, creative and format design and production, and postal product and supplier advice.

We believe there is scope for OGCBuying.solutions to use their set-up of the postal services frameworks as a template for future frameworks, and if similarly managed, the agency, and the public sector in general, can realise significant benefits from future work.

13 We will, during the course of 2006, be seeking to promote the key messages in this report across the public sector and to support this by developing a range of subsidiary efficiency based tools for use by public sector organisations. For example, we have developed a *postal efficiency improvement tree* to assist public sector organisations in determining the most efficient procurement approach and the postal services and products that might offer the best value (**Figure 3 on page 9**). The *tree* provides a set of options to:

- reduce the cost of service, through demand management, reduced cost per unit, and improved management structures; and
- improve the quality and effectiveness of their post.

The tool can be read 'left-to-right' with each step detailing how the objective can be met and also 'right-to-left' to capture the business objectives behind particular actions and tactics to improve postal efficiency. The associated volumes to this report describe how public and private sector organisations have implemented these actions and the financial and service delivery benefits they have achieved.

2 Actions which departments need to take to further improve their postal services performance

Areas where public sector organisations need to make more progress

Post is not always considered as part of an integrated communication strategy.

Departments often have various, disjointed strategies governing their communications with citizens, particularly in those departments comprised of multiple businesses. These strategies sometimes consider communication channels in isolation of each other, increasing the likelihood that opportunities to reduce demand for mail and increase staff productivity will be missed.

Management structures for postal services are often too fragmented. Postal services span many areas of the business, including marketing, operations, procurement, and customer service. These areas need to be brought together to deliver the most impact to postal service efficiency initiatives.

Recommendations

A Departments need to develop an integrated communication and commercial strategy which will require them to:

- i plan and implement communication strategies across their business as a whole, identifying the optimal mix of communication methods to best meet the needs of customers, maximise the productive time of staff, and reduce procurement costs. This will include certain scenarios where post is the most appropriate communication channel;
- ii produce joint plans by those responsible for communications and procurement;
- iii challenge the demand for inbound and outbound mail;
- iv review postal requirements and operations within a wider communication, production, and delivery value chain.

B Develop capable and effective management structures for postal services, including:

- i establishing clear accountabilities and responsibilities for the initiation, implementation and monitoring of postal initiatives;
- ii developing relationships between the postal team and other areas of the business;
- iii staff with expert knowledge of procuring in the postal market;
- iv identifying opportunities to centralise processing of output and inbound mail.

Examples of where this has been achieved

Strathclyde Police needed to supplement traditional information gathering techniques in the investigation of a serious violent crime. In consultation with Royal Mail and the Central Office of Information, they targeted a specific, hard-to-reach, geographic area in Glasgow using direct mail to seek further information on the incident. **This use of direct mail had significant time and cost savings as compared with officers canvassing individual households, increased public reassurance, and acquired valuable information on the circumstances of the crime.**

National Savings and Investments has reduced its demand for mail through a change in policy where Individual Savings Account statements are sent bi-yearly rather than quarterly. **It has achieved an annual saving of some £90,000 as a result.**

The Department for Work and Pensions' Pension Service, in response to a survey stating that 75 per cent of customers would prefer transacting over the phone, has begun to accept applications for State Pensions by telephone. **The change is expected to reduce the amount of inbound post by 60 per cent, from 650,000 new applications received per year to 260,000, bringing about significant productive time savings.**

The Department of Work and Pensions' Debt Management business' ten sites used to print and dispatch mail at each individual site. In 2004, the business implemented a centralised print service through which 2.5 million items of mail were printed and dispatched in 2005. **This shared service across ten sites has enabled the business to aggregate its print throughput and take advantage of discounted mail products resulting in estimated savings of £80,000.**

2 Actions which departments need to take to further improve their postal services performance *continued*

Areas where public sector organisations need to make more progress

Opportunities for efficiency through better market and supplier engagement and aggregation with other departments are often missed. There are few examples within the public sector of organisations using alternative suppliers to Royal Mail, using external providers, for example for mail printing or sorting, and accessing the power of aggregated purchasing and production across single departments and jointly with others. Departments need to do more to assess whether the economies of scale outweigh the costs of joint requirements gathering, co-ordinated communications planning, operational changes, and integration of IT systems.

Reduce the volume of mail that cannot be delivered to the addressee because of incorrect address information. Departments do not consistently maintain up-to date customer address information, resulting in unnecessary postage, printing, and processing costs. Improving customer data has benefits that lie outside of postal procurement such as avoiding the costs of customers contacting the organisation because mail has not arrived, improved effectiveness of customer processes (for example, debt management), and better customer service.

Recommendations

C Use the appropriate procurement and supplier engagement practices through:

- i a clear understanding of the business requirements and communication objectives for post;
- ii engagement with the market place to work with suppliers and survey market intelligence;
- iii consideration of alternative suppliers and engagement, if appropriate, using the OGCbuying.solutions framework agreements;
- iv establishing effective incentives and actively managing contracts;
- v assessing whether specific in-house postal activities can be more efficiently done by external providers.

D Aggregate demand and increase joint working wherever possible within departments and with others, in particular through:

- i joint contract management;
- ii joint communication strategies (where departments send mail to the same customers);
- iii sharing of customer information (for example, on change of address);
- iv shared services for production and dispatch of mail.

E Improve the accuracy and management of customer address data by use of external data files (such as the Postcode Address File) to:

- i check outbound addresses and customer information before mail is sent;
- ii use 'undeliverable' information from suppliers and customers to update systems.

Examples of where this has been achieved

The RBS Group was the first major customer of Royal Mail to develop and implement 'Downstream Access' for its bulk mail output. **In 2005, RBS despatched over 200 million envelopes via Downstream Access¹ generating net incremental savings of some seven percent of total postage spend², along with better customer service through quicker delivery for a considerable proportion of their customers.**

HM Revenue and Customs began closer scrutiny of their postal contracts following the set-up of their central post team in 2003. **The department estimates that this team has made contract management savings of £700,000.**

HM Revenue and Customs and the Department for Work and Pensions have agreed a joint contract for courier services as the two departments often have sites close together to each other and require high volumes of mail to be sent between their own and each other's sites. Their joint contract covers inter-office recorded and non-recorded next day delivery. The contract has been let in such a manner to allow additional departments to be included. The key benefit of this joint contract is reduced costs for contract management and tendering and lower prices and **the Department for Work and Pensions has estimated the savings at £1.8 million per year.**

National Savings and Investments' direct marketing outsourcer has implemented a series of data processing steps to improve their address data quality. **In a direct marketing campaign in September 2005, the redesigned process saved some £20,000 in postage costs as well as printing and processing savings, and improved customer satisfaction as customers did not receive multiple, potentially conflicting, marketing messages from the agency.**

2 Actions which departments need to take to further improve their postal services performance *continued*

Areas where public sector organisations need to make more progress

Mail products which do not represent the closest fit to communication and cost-efficiency requirements are sometimes chosen. Departments do not make best use of postal products, in particular those products offering discounts to the customer in return for performing basic mail preparation tasks, such as address sorting, and lower-cost, reduced timeliness products.

Supplier and internal performance information is not systematically gathered and used as the basis for postal services procurement and management decisions.

Departments do not gather sufficient information on supplier or internal performance, particularly on spend and products to enable smarter supplier and product choice.

Recommendations

F Select the appropriate mail products, balancing business requirements with cost and quality of customer service, requiring:

- i better use of delivery products with alternative timings such as second class or two-day mail;
- ii increased use of 'work share'³ products;
- iii a change in mail formats;
- iv use of the most appropriate payment method;
- v better use of high quality postal products.

G Increase the availability and use of management information to improve postal efficiency and service delivery, by:

- i collecting data on spend by product type and team;
- ii benchmarking services;
- iii collecting and analysing data on quality of service indicators.

Examples of where this has been achieved

The Driver and Vehicle Licensing Agency has implemented a combination of software and mechanical sorting equipment at their main processing sites to increase the volume of mail qualifying for postal volume discounts to levels that compare favourably with leading private sector companies. **The approach is achieving annual savings of some £3 million.**

HM Revenue and Customs increased its use of second class and products with longer delivery timescales for the dispatch of New Tax Credit newsletters in 2004-05. **The estimated savings for the year is £1.3 million.**

The Department for Work and Pensions has chosen to replace standard tariff first class mail with a second class 'work share' product for its Winter Fuel payments and correspondence in 2005-06, while remaining within end-to-end service levels. **The use of second class mail saved the department an estimated £1.2 million, without any adverse customer reaction.**

The Higher Education Purchasing Group for Postal Services collates data from suppliers as well as from member institutions to produce progress reports on the use of their contracts. **It has used these reports to demonstrate to member institutions that they were able to get better prices and service quality by transferring onto the national contracts.**

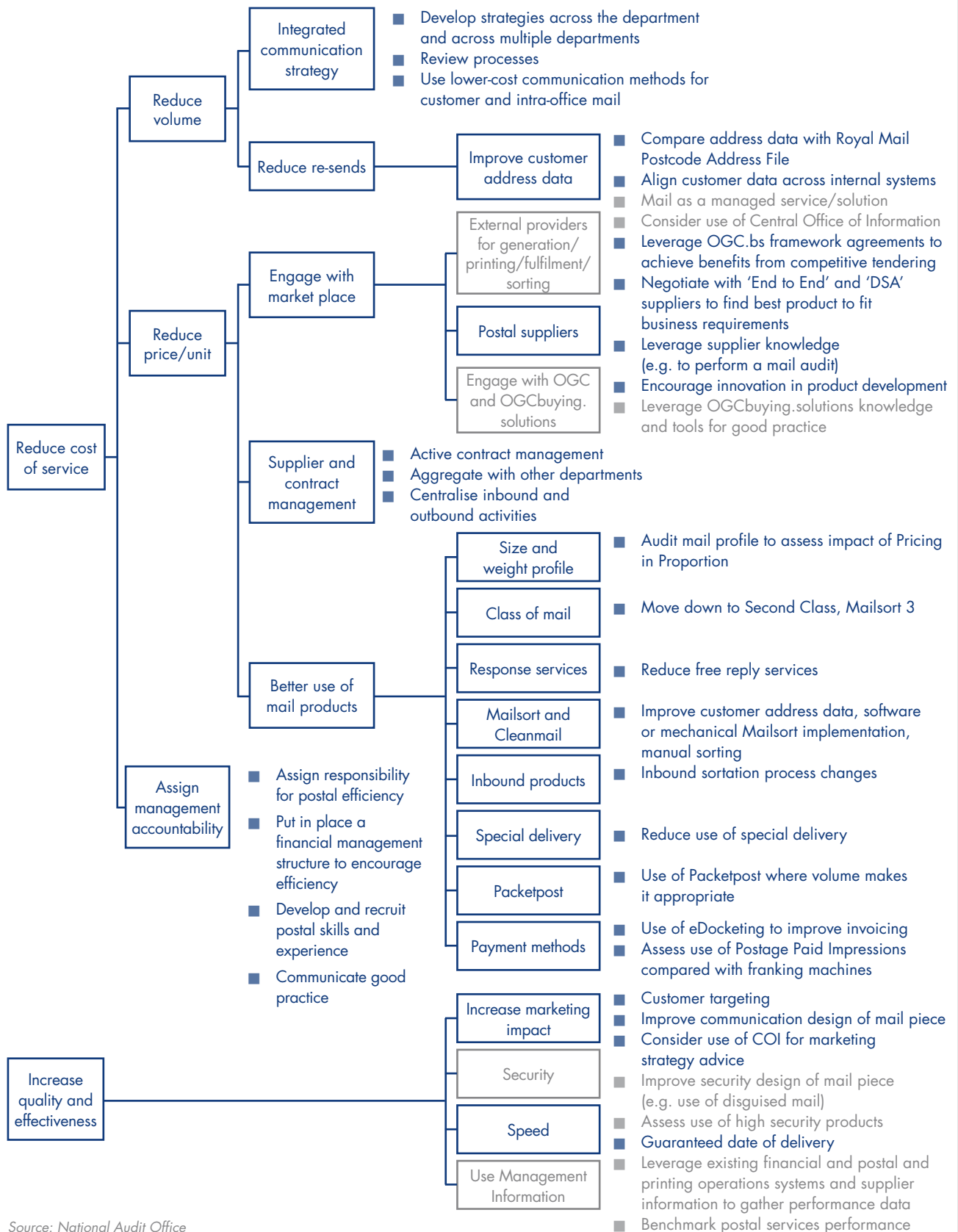
The Driver and Vehicle Licensing Agency is provided information by Royal Mail to allow them **to compare the service quality provided for its mail specifically against national benchmarks** to assess whether end-to-end service levels are being met.

Source: National Audit Office

NOTES

- 1 Downstream Access is where postal companies other than Royal Mail collect mail from customers before injecting the mail into Royal Mail's supply chain for final delivery.
- 2 The net savings are gross savings less trunking costs.
- 3 Postal 'worksharing' involves customers performing activities such as preparing or sorting mail, often by geographic areas, and thus receiving discounts from suppliers.

3 Postal efficiency improvement tree



Source: National Audit Office