

ROYAL MAIL WHOLESALE

ACCESS CONTRACT CHANGE PROPOSAL

A NEW WAY OF CALCULATING THE URBAN DENSITY MEASURE OF NATIONAL PRICE PLAN ONE (SSCS)

8 June 2017

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Introduction

In September 2016, we consulted on a variety of change proposals related to addressing arbitrage between the price plans of the Access Letters Contract and the Wholesale Parcels Contract. One of those proposals related to a change to the way we measure the Urban Density Benchmark under National Price Plan One (SSCs) (NPP1) to make it a more accurate monitor of urban mail.

From the customer feedback we received from the September 2016 consultation and the more recent customer workshop that we held on 6 April 2017, the majority of customers are supportive of us making the change to the Urban Density methodology. We have however noticed a flaw in the methodology that we proposed in September 2016. We shared the detail of the flaw and proposed an amendment to the calculation to address it with the customers that attended the April customer workshop. The customers at the workshop suggested that we re-consult on the Urban Density proposal. Hence this consultation seeks customer views on our slightly amended Urban Density calculation.

We welcome feedback from all customers and in particular seek the views of NPP1 customers.

Current Urban Density methodology

The current methodology measures the volume of urban mail at each SSC and expresses it as a percentage of total urban mail volumes for all SSCs so that the sum percentage of all SSCs equals 100%.

A key flaw of this methodology is that if customers remove urban mail volume proportionately across all SSCs, they will still meet the Urban Density Benchmark. This means a customer can remove urban mail without incurring any adjustments which clearly defeats the purpose of the measure.

From our September 2016 consultation on measures to address arbitrage, and the April 2017 customer workshop, we know that customers are supportive of us changing this methodology.

Proposed new Urban Density methodology

We propose to change the way we measure Urban Density under NPP1 for all customers. The new methodology would measure the volume of urban mail at each SSC and express it as a percentage of total volume for each SSC. We would allow a Permitted Variance of 40% for each SSC.

Figure 1: Proposed new Urban Density methodology

For simplicity, the permitted variance is set to 0%	Customer Actual Volume	UD Benchmark	Target Urban Volume	% urban volume outside Benchmark
Urban mail in SSC xxx	50	40%	40	-10%
Other mail in SSC xxx	50	Note: negative implies surplus items, no adjustment charge incurred		
Total mail in SSC xxx	100			

This is the proposal we consulted on in September 2016. The benefit of this methodology is that the urban mail profile of any one SSC is measured independently of other SSCs, avoiding any distortive effect. Each SSC has its own urban density profile, and we assess actual urban volume against that profile.

At the time of the September 2016 consultation, we shared the impact analysis with each individual NPP1 customer and used the following calculation to determine whether the customer's profile incurred any adjustments:

Sep 2016 calculation:

% urban volume outside Benchmark x Customer actual urban volume in SSC = Adjustment volume

e.g. (using Figure 1's example SSC): $-10\% \times 50 = -5$

This calculation is incorrect because the adjustment volume does not bring the volume back to match the target volume. In the example above, the adjustment volume of -5 only brings the customer's urban mail volume in the SSC back to 45 ($50 - 5$) when the target urban mail volume for that SSC is 40 (see Figure 1).

Instead of multiplying the SSC percentage shortfall or surplus of urban items by the urban volume, the correct calculation is to multiply the percentage shortfall or surplus of urban items by the total volume of all items at that SSC, as illustrated below:

Revised calculation:

% urban volume outside Benchmark x Customer Total mail in SSC = Adjustment volume

e.g. (using Figure 1's example SSC): $-10\% \times 100 = -10$

Unlike the September 2016 calculation, the revised calculation accurately calculates the volume of urban mail that would be required to meet the target urban mail volume. It is also a fair calculation because, unlike the September 2016 calculation, it prevents customers from removing all of their urban volume from an SSC and avoiding adjustment charges.

Timing

Subject to customer feedback, we propose to adopt the new Urban Density methodology and calculation from the start of the next contract year, 26 March 2018.

Questions:

1. Do you have any comments in response to the proposed new Urban Density methodology and calculation?
2. Do you have any comments in response to changing to the new Urban Density methodology from the start of the next contract year?

Please send your comments to Luisa Fulci at Luisa.fulci@royalmail.com by **21 July 2017**.