



Proposed changes to Royal Mail's Costing Manual

Consultation

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Section 1

Executive Summary

- 1.1 Under the Initial Conditions¹, Royal Mail Group Ltd ("Royal Mail") must seek Ofcom's approval to make material changes to its costing methodology for regulatory reporting purposes, as set out in its Costing Manual².
- 1.2 The Initial Conditions require Ofcom to assess whether the changes are consistent with the Costing Methodology Guiding Principles³ and the Methodological Principles⁴. If we are satisfied that the changes are consistent with such principles, we are required to provide our consent to the proposed change by direction in writing. Our consent though, is subject to a statutory consultation period of 1 month.
- 1.3 Royal Mail has proposed certain changes to its Costing Manual. In this consultation we present the proposed changes and explain why we consider the changes are, in our view, consistent with both the Costing Methodology Guiding Principles and the Methodological Principles. We also propose to give our consent to the changes by direction in writing.
- 1.4 Before reaching a final decision, we are consulting on Royal Mail's proposed changes. In particular, we are seeking stakeholders' views on whether each of the proposed changes are consistent with;
 - the Costing Methodology Guiding Principles; and
 - the Methodological Principles
- 1.5 In light of the consultation responses we receive, we will make a final decision as to whether we will consent to the proposed changes by direction in writing, or whether we shall notify Royal Mail that the change(s) is/are inconsistent with the Costing Methodology Guiding Principles and/or the Methodological Principles.

Impact Assessment

- 1.6 Under the Communications Act 2003, we are required to carry out an impact assessment where a proposal in connection with the carrying out of our functions is "important". A proposal is "important" if its implementation is likely to involve a major change in the activities carried on by Ofcom or have a significant impact on persons carrying on business in the markets we regulate, or the general public. We do not consider that the proposals in this consultation paper are "important" in this sense.

Timetable

- 1.7 Responses to the consultation and question raised in Annex 4 are due by 5pm on Friday 18 May 2012.

¹ The regulatory conditions imposed on postal operators by Ofcom pursuant to Section 66 and Paragraphs 4 to 6 of Schedule 9 of the Act for a transitional period

² The document which gives a detailed description of Royal Mail's costing methodology and sources of data

³ The principles as set out in the Annex to Acc 1 of the Initial Conditions

⁴ The principles set out in Appendix D of the document published by the Postal Services Commission in March 2011 entitled "Laying the foundations for a sustainable postal service"

- 1.8 We aim to publish a statement following consideration of stakeholders' responses as soon as possible thereafter.

Section 2

Royal Mail's proposed costing methodology changes for 2011/12

Introduction

- 2.1 Royal Mail is a postal operator which was designated to be the universal service provider.
- 2.2 Pursuant to Section 66 and Paragraphs 4 to 6 of Schedule 9 of the Postal Services Act 2011 (the "Act") and by statement of 29 September 2011⁵, Ofcom set regulatory conditions and directions to apply to postal operators for a transitional period. Such conditions (known as the "Initial Conditions") included, amongst others, the universal service provider accounting conditions.
- 2.3 Under accounting condition ("Acc") 1.3, Royal Mail as the universal service provider is required to maintain a Costing Manual. The Costing Manual is a document which gives a detailed description of the costing methodology and sources of data used by Royal Mail to prepare the regulatory financial statements as required by Ofcom. Such Costing Manual can only be modified in accordance with the procedure set out in the accounting conditions. In particular, any change which amounts to a Material Change (as defined in the universal service provider accounting conditions) is subject to Ofcom's consent. Ofcom shall only consent to a proposed change if the proposed change is consistent with the Costing Methodology Guiding Principles⁶ and the Methodological Principles⁷. Any consent is however subject to a statutory consultation period of 1 month, in accordance with Paragraph 4 of Schedule 6 to the Act.
- 2.4 In February 2012, Royal Mail informed Ofcom that it was looking to amend its Costing Manual in a number of respects. On 23 March 2012, Royal Mail published an update version of its Costing Manual ("ABC Costing Manual 2011-12 Version 2011-3")⁸. Appendix D of this Costing Manual refers to these proposed changes. On 27 March 2012, Ofcom published its decision on the new regulatory framework for Royal Mail ("Securing the Universal Postal Service - Decision on the regulatory framework")⁹ where in paragraph 11.45 Ofcom referred to these Costing Manual changes and in paragraph 11.47 stated that "*we shall shortly commence the required one month's statutory consultation over the changes*". This is the consultation referred to in paragraph 11.47.
- 2.5 In this consultation we present the proposed changes, and explain why we consider the changes are, in our view, consistent with both the Costing Methodology Guiding

⁵ <http://stakeholders.ofcom.org.uk/binaries/consultations/postal-regulation/statement/statement.pdf>

⁶ See the Annex to Condition Acc 1, page 32 of the statement of 29 September 2011 available at <http://stakeholders.ofcom.org.uk/binaries/consultations/postal-regulation/statement/statement.pdf>

⁷ See Appendix D of the document published by the Postal Services Commission in March 2011 entitled "Laying the foundations for a sustainable postal service", available at <http://stakeholders.ofcom.org.uk/binaries/post/1878.pdf>

⁸ [http://www.royalmailgroup.com/sites/default/files/Costing%20Manual%20%20v2011-3V\(625KB\).pdf](http://www.royalmailgroup.com/sites/default/files/Costing%20Manual%20%20v2011-3V(625KB).pdf)

⁹ <http://stakeholders.ofcom.org.uk/binaries/consultations/review-of-regulatory-conditions/statement/statement.pdf>

Principles and the Methodological Principles, and invite stakeholders to comment on our analysis.

- 2.6 It should be noted that this consultation is required by the universal service provider accounting conditions set out in the Initial Conditions, which only apply for the financial year beginning 28 March 2011. The regulatory reporting regime which takes effect from April 2012, including requirements for changes to Royal Mail's costing methodology, was set out in our Statement "Securing the Universal Postal Service Decision on the new regulatory framework" published on 27 March¹⁰. The rules for the costing methodology to be used by Royal Mail are now outlined in the universal service provider accounting conditions and the Regulatory Accounting Guideline (RAG) published within this statement. This new regulatory reporting regime will not require Ofcom's prior consent for changes to the Costing Manual.

Proposed changes to Royal Mail's costing methodology

Regional Distribution Centre Accommodation

- 2.7 Royal Mail has proposed that a new costing method should be applied to perform the cost allocation of shared space within the Regional Distribution Centres (RDCs).
- 2.8 Previously, RDC accommodation costs were recovered according to measured utilised processing space and did not include 'shared space' (e.g. staff facilities). The new costing method is more detailed and identifies: utilised space according to specific RDC product groups, various operational and staff space categories, and in some cases spare space. The shared space is now attributed to the RDC product groups based on the actual accommodation area that the processing of the product utilises which is then marked up with a measurement of the actual accommodation area that is 'shared space'.

Regional Distribution Centre Mail Handling Equipment

- 2.9 Royal Mail has proposed that a new cost driver for the attribution of RDC Mails Handling Equipment ("MHE") should be applied.
- 2.10 The mail processed within the RDCs is presented and/or moved in containers. These containers are processed within the RDC unit using MHE; various different container movements occur within the RDC (e.g. bulk mail in cages moved by fork-lift, unsorted packets moved by conveyor). The costs associated with the MHE were previously attributed to the product groups based on staff hours required to process the different product groups. The costs are now to be attributed to the product groups based on accommodation costs for each of the product groups. The assumption is that accommodation space better reflects the requirement for the handling of mail containers in the RDC.

Pipeline segment changes

- 2.11 Royal Mail is proposing to re-classify three activities from one part of its operational pipeline to another.

¹⁰ <http://stakeholders.ofcom.org.uk/binaries/consultations/review-of-regulatory-conditions/statement/statement.pdf>

2.12 The three re-classifications are given below:

- The activity recording, primarily, the cost of staff uniforms was previously mapped to the 'Network Distribution' area of the pipeline and is to be moved to the 'Support' process.
- The activity recording the costs of the 'Sameday' service was previously mapped to the 'Network Distribution' area of the pipeline and is to be moved to the 'Royal Mail Specialist Service' process.
- The activity recording the consolidation and segregation of bulk mail has been identified as being wholly used for the interception of 1400 mail (Mailsort, Wholesale and Spring) for input to the Walk Sorting Machines and therefore is to be moved from the collection process to the Inward Mail Centre part of the pipeline.

Summary of changes

2.13 The following table represents a summary of the changes proposed by Royal Mail showing the costing change, existing methodology and the proposed methodology.

<i>Costing Change</i>	<i>Existing Methodology</i>	<i>Proposed Methodology</i>
Regional Distribution Centre Accommodation Costs	Costs allocated using measured utilised processing space	Costs allocated using utilised space, operational and staff space and spare space
Regional Distribution Centre Mail Handling Equipment Costs	Costs allocated based on staff hours	Costs allocated based on accommodation space
Pipeline Segment Change: staff uniforms activity	Activity mapped to the 'Network Distribution' area of the pipeline	Activity mapped to the 'Support' process of the pipeline
Pipeline Segment Change: 'sameday' service activity	Activity mapped to the 'Network Distribution' area of the pipeline	Activity mapped to the 'Royal Mail Specialist Service' process of the pipeline
Pipeline Segment Change: consolidation and segregation of bulk mail activity	Activity mapped to the 'Collection' process of the pipeline	Activity mapped to the 'Inward Mail Centre' part of the pipeline

Ofcom assessment of the proposed changes

Material Change

2.14 We have explained above that the Initial Conditions require Ofcom's consent to change the Costing Manual where a change is "material".

2.15 A "material change" has the meaning given to it in under Acc 1.20 which states:

"a Material Change means any change to which Principle 17(b) of the Methodological Principles applies, such that: (a) the numerical consequence of any such change exceeds the threshold for materiality set out in Principle 17(b) of the Methodological Principles; or (b) that change is a Connected Change in relation to other changes that have been made or the Universal Service Provider is planning to make in the relevant quarter or has made during the previous quarter (in the same financial year), and the combined value of which exceeds the threshold for materiality set out in Principle 17(b) of the Methodological Principles."

Principle 17(b) of the Methodological Principles (as set out in Appendix D of the document published by the Postal Services Commission in March 2011 entitled "Laying the foundations for a sustainable postal service")¹¹ states:

"Any change to the Royal Mail product Costing Manual will be deemed to be material if:

- *There is a resultant percentage change (be it positive or negative) in the total cost of any Activity set out in the Costing Manual that exceeds 1%;*
- *There is a resultant percentage change (be it positive or negative) in the total cost of any Sub-product set out in the Costing Manual that exceeds 1%; and*
- *There is a resultant percentage change (be it positive or negative) in the unit cost of any Sub-product set out in the Costing Manual that exceeds 1%.*

The resultant percentage change shall be calculated by taking the cost of each Sub-product or Activity without the change ("Base Cost") and subtracting that Base Cost from the corresponding cost of each Sub-product or Activity with the change and dividing this result by the Base Cost.

Materiality shall be measured by reference to the most recent quarterly accounts provided that where Royal Mail can justify a longer period as being more representative, then, such longer period may be used."

A Connected Change is defined in the Initial Conditions as:

"any change to the Costing Manual which when taken together with one or more other changes to the Costing Manual could reasonably be considered by Ofcom to amount substantively to a single change to the Costing Manual that would be considered to be a Material Change under Condition Acc 1.20."

2.16 We have considered the impact of each of the proposed changes on Royal Mail's costs and on the basis of the above criteria are satisfied that each of the changes are

¹¹ <http://stakeholders.ofcom.org.uk/binaries/post/1878.pdf>

material. Accordingly, we have assessed whether each change is compliant with both the Costing Methodology Guiding Principles and the Methodological Principles for Product Costing.

The Regional Distribution Centre Accommodation change

- 2.17 Ofcom has considered the proposed change in light of each and every principle set out in the Costing Methodology Guiding Principles and the Methodological Principles. We believe that the proposed change is consistent with all these principles. For this proposed change, we consider that the following principles are particularly relevant.
- 2.18 Costing Methodology Guiding Principle 4 'Objectivity' states that "*each element of the Costing Methodology must, as far as possible, be based on, or take account of all the available financial and operational data that is relevant to that element.*" We believe that the proposed change is consistent with this principle, as the new assessment of facilities utilisation involved is a more comprehensive assessment of the relevant operational data used for costing, and it collects various assessments of RDC space activities which were previously not collected by Royal Mail.
- 2.19 Our assessment is that the proposed change to the new measurement methodology is also consistent with Costing Methodology Guiding Principle 7 'Consistency'. The principle states amongst others that "*as far as possible, the Costing Methodology must be applied consistently over time*". Ofcom considers that this principle should not be interpreted so strictly as to disallow this change as it would make the costing system too rigid in process terms and inflexible to any new, valid methods of treatment. In particular, it is also relevant here to refer to Methodological Principle 15 'Operational data and sampling' which states amongst others that "*All operational data used by the Costing Methodology must be regularly reviewed and where necessary updated to ensure the accuracy of costing and its consistency with the operational reality (Principle 3 'Operational Reality').*"

The Regional Distribution Centre Mail Handling Equipment change

- 2.20 Ofcom has considered the proposed change in light of each and every principle set out in the Costing Methodology Guiding Principles and the Methodological Principles. We believe that the proposed change is consistent with all these principles. For this proposed change, we consider that the Costing Methodology Guiding Principles 3 and 7 and Methodological Principle 7 are particularly relevant.
- 2.21 Royal Mail has explained that the proposed change from the use of staff hours to accommodation space to attribute the MHE costs is because this is a better reflection of the utilisation of MHE in the RDC, in the absence of readily available operational measurements of actual container movements by product group.
- 2.22 Costing Methodology Guiding Principle 3 'Causality' states that "*The Costing Methodology must assign General Ledger costs to Activities that cause those costs to be incurred. The Costing Methodology must assign Activity Costs to those Sales Products that are provided as a result, or are supported by, those Activities.*" We believe the proposed change is consistent with this principle as the use of accommodation space as the new driver chosen is likely to reasonably reflect the utilisation of Mail Handling Equipment and their associated costs.

- 2.23 Our assessment is that the proposed change to the accommodation driver is consistent with Methodological Principle 7 'Resource Drivers' as it appropriately reflects the resource consumption giving rise to the cost of the MHE utilisation within the RDC.
- 2.24 We believe that the proposed change is consistent with Costing Methodology Guiding Principle 7 'Consistency'. We have already indicated above that this principle should not be interpreted so strictly as to disallow a change as it would make the costing system too rigid in process terms and inflexible to any new, valid methods of treatment and in particular that Methodological Principle 15 'Operational data and sampling' also requires that *"All operational data used by the Costing Methodology must be regularly reviewed and where necessary updated to ensure the accuracy of costing and its consistency with the operational reality (Principle 3 'Operational Reality')"*.

The Pipeline segment changes

- 2.25 Ofcom has considered each of the proposed changes in light of each and every principle set out in the Costing Methodology Guiding Principles and the Methodological Principles. We believe that each of the proposed changes are consistent with these principles. For these proposed changes, we consider that Methodological Principle 3 'Operational Reality' is particularly relevant.
- 2.26 Methodological Principle 3 'Operational Reality' states that *"As far as practicable, the Costing Methodology must reflect the operations of Royal Mail as they are undertaken."* Ofcom's assessment is that each of Royal Mail's three proposed pipeline changes reflects the pipeline segment with which the activity cost should be identified.

Legal tests

- 2.27 For the reasons set out above, we propose to give our consent to the proposed changes by direction.
- 2.28 In making this proposal, Ofcom considers it is acting in accordance with its principal duty in section 29 of the Act and its general duties in section 3 of the Communications Act 2003.
- 2.29 We have set out below our assessment of how our proposed direction meets the specific legal tests set out in the Act, and in particular, the requirements set out in Paragraph 4(2) of Schedule 6 of the Act that we may only give a direction if we are satisfied that the direction:
- i) is objectively justifiable;
 - ii) does not discriminate unduly against particular persons or a particular description of persons;
 - iii) is proportionate to what it is intended to achieve; and
 - iv) is transparent in relation to what it is intended to achieve.
- 2.30 Ofcom considers that giving our consent to the proposed changes by direction is objectively justifiable, because we have verified that the proposed changes are consistent with the Costing Methodology Guiding Principles and the Methodological Principles, and we have found them to be so.

- 2.31 Ofcom considers that giving our consent to the proposed changes by direction does also not discriminate unduly against particular persons or a particular description of persons, as the obligation to maintain a Costing Manual, and the processes to modify such Costing Manual, apply to the universal service provider (i.e. Royal Mail) only.
- 2.32 Ofcom further believes that the direction whereby we give our consent to the proposed changes is proportionate to what it is intended to achieve. The accounting conditions relating to the Costing Manual seek to ensure that the costing methodology and sources of data used in financial and accounting records of the universal service provider are described in a detailed manner, which ensures consistent financial records, and a better understanding by its readers. Changes may need to be made to the Costing Manual to ensure the financial records are fit for purpose. The proposed direction is no more than necessary to ensure that the accounting and financial records of the Universal Service Provider are fit for purpose.
- 2.33 Finally, Ofcom also believes the direction is transparent in relation to what it is intended to achieve. Ofcom has described the proposed changes and why we believe they are consistent with the Costing Methodology Guiding Principles and the Methodological Principles in this consultation document.

Question

Do you consider that each of the proposed changes are consistent with the Costing Methodology Guiding Principles and the Methodological Principles? If you do not consider the proposed changes to be consistent with the Costing Methodology Guiding Principles or the Methodological Principles, please explain with which Principle(s) the proposed changes is/are inconsistent and why.

Annex 1

Responding to this consultation

How to respond

- A1.1 Ofcom invites written views and comments on the issues raised in this document, to be made **by 5pm on 18 May 2012**.
- A1.2 Ofcom strongly prefers to receive responses using the online web form at <https://stakeholders.ofcom.org.uk/consultations/royal-mails-costing-manual/howtorespond/form>, as this helps us to process the responses quickly and efficiently. We would also be grateful if you could assist us by completing a response cover sheet (see Annex 3), to indicate whether or not there are confidentiality issues. This response coversheet is incorporated into the online web form questionnaire.
- A1.3 For larger consultation responses - particularly those with supporting charts, tables or other data - please email kamak.arzhangj@ofcom.org.uk attaching your response in Microsoft Word format, together with a consultation response coversheet.
- A1.4 Responses may alternatively be posted or faxed to the address below, marked with the title of the consultation.
- Kamak Arzhangj
Ofcom
Riverside House
2A Southwark Bridge Road
London SE1 9HA
- Fax: 020 7783 4109
- A1.5 Note that we do not need a hard copy in addition to an electronic version. Ofcom will acknowledge receipt of responses if they are submitted using the online web form but not otherwise.
- A1.6 It would be helpful if your response could include a direct answer to the question asked in this document, which is given at Annex 4. It would also help if you can explain why you hold your views and how Ofcom's proposals would impact on you.

Further information

- A1.7 If you want to discuss the issues and questions raised in this consultation, or need advice on the appropriate form of response, please contact Kamak Arzhangj on 020 7783 4339.

Confidentiality

- A1.8 We believe it is important for everyone interested in an issue to see the views expressed by consultation respondents. We will therefore usually publish all responses on our website, www.ofcom.org.uk, ideally on receipt. If you think your response should be kept confidential, can you please specify what part or whether

all of your response should be kept confidential, and specify why. Please also place such parts in a separate annex.

- A1.9 If someone asks us to keep part or all of a response confidential, we will treat this request seriously and will try to respect this. But sometimes we will need to publish all responses, including those that are marked as confidential, in order to meet legal obligations.
- A1.10 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use. Ofcom's approach on intellectual property rights is explained further on its website at <http://www.ofcom.org.uk/about/accoun/disclaimer/>

Next steps

- A1.11 Following the end of the consultation period, Ofcom intends to publish a statement shortly thereafter.
- A1.12 Please note that you can register to receive free mail Updates alerting you to the publications of relevant Ofcom documents. For more details please see: http://www.ofcom.org.uk/static/subscribe/select_list.htm

Ofcom's consultation processes

- A1.13 Ofcom seeks to ensure that responding to a consultation is easy as possible. For more information please see our consultation principles in Annex 2.
- A1.14 If you have any comments or suggestions on how Ofcom conducts its consultations, please call our consultation helpdesk on 020 7981 3003 or e-mail us at consult@ofcom.org.uk. We would particularly welcome thoughts on how Ofcom could more effectively seek the views of those groups or individuals, such as small businesses or particular types of residential consumers, who are less likely to give their opinions through a formal consultation.
- A1.15 If you would like to discuss these issues or Ofcom's consultation processes more generally you can alternatively contact Graham Howell, Secretary to the Corporation, who is Ofcom's consultation champion:

Graham Howell
Ofcom
Riverside House
2a Southwark Bridge Road
London SE1 9HA

Tel: 020 7981 3601

Email Graham.Howell@ofcom.org.uk

Annex 2

Ofcom's consultation principles

A2.1 Ofcom has published the following seven principles that it will follow for each public written consultation:

Before the consultation

A2.2 Where possible, we will hold informal talks with people and organisations before announcing a big consultation to find out whether we are thinking in the right direction. If we do not have enough time to do this, we will hold an open meeting to explain our proposals shortly after announcing the consultation.

During the consultation

A2.3 We will be clear about who we are consulting, why, on what questions and for how long.

A2.4 We will make the consultation document as short and simple as possible with a summary of no more than two pages. We will try to make it as easy as possible to give us a written response. If the consultation is complicated, we may provide a shortened Plain English Guide for smaller organisations or individuals who would otherwise not be able to spare the time to share their views.

A2.5 We will consult for up to 10 weeks depending on the potential impact of our proposals.

A2.6 A person within Ofcom will be in charge of making sure we follow our own guidelines and reach out to the largest number of people and organisations interested in the outcome of our decisions. Ofcom's 'Consultation Champion' will also be the main person to contact with views on the way we run our consultations.

A2.7 If we are not able to follow one of these principles, we will explain why.

After the consultation

A2.8 We think it is important for everyone interested in an issue to see the views of others during a consultation. We would usually publish all the responses we have received on our website. In our statement, we will give reasons for our decisions and will give an account of how the views of those concerned helped shape those decisions.

Annex 3

Consultation response cover sheet

- A3.1 In the interests of transparency and good regulatory practice, we will publish all consultation responses in full on our website, www.ofcom.org.uk.
- A3.2 We have produced a coversheet for responses (see below) and would be very grateful if you could send one with your response (this is incorporated into the online web form if you respond in this way). This will speed up our processing of responses, and help to maintain confidentiality where appropriate.
- A3.3 The quality of consultation can be enhanced by publishing responses before the consultation period closes. In particular, this can help those individuals and organisations with limited resources or familiarity with the issues to respond in a more informed way. Therefore Ofcom would encourage respondents to complete their coversheet in a way that allows Ofcom to publish their responses upon receipt, rather than waiting until the consultation period has ended.
- A3.4 We strongly prefer to receive responses via the online web form which incorporates the coversheet. If you are responding via email, post or fax you can download an electronic copy of this coversheet in Word or RTF format from the 'Consultations' section of our website at www.ofcom.org.uk/consult/.
- A3.5 Please put any parts of your response you consider should be kept confidential in a separate annex to your response and include your reasons why this part of your response should not be published. This can include information such as your personal background and experience. If you want your name, address, other contact details, or job title to remain confidential, please provide them in your cover sheet only, so that we don't have to edit your response.

Cover sheet for response to an Ofcom consultation

BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

CONFIDENTIALITY

Please tick below what part of your response you consider is confidential, giving your reasons why

Nothing

☐

Name/contact details/job title

☐

Whole response

☐

Organisation

☐

Part of the response

☐

If there is no separate annex, which parts?

If you want part of your response, your name or your organisation not to be published, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response that Ofcom can publish. However, in supplying this response, I understand that Ofcom may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations. If I have sent my response by email, Ofcom can disregard any standard e-mail text about not disclosing email contents and attachments.

Ofcom seeks to publish responses on receipt. If your response is non-confidential (in whole or in part), and you would prefer us to publish your response only once the consultation has ended, please tick here.

☐

Name

Signed (if hard copy)

Annex 4

Consultation question

Do you consider that each of the proposed changes are consistent with the Costing Methodology Guiding Principles and the Methodological Principles? If you do not consider the proposed changes to be consistent with the Costing Methodology Guiding Principles or the Methodological Principles, please explain with which Principle(s) the proposed changes is/are inconsistent and why.

Annex 5

Notification of a proposed consent by direction under Acc 1.16 of the Initial Conditions

Notification of a proposed consent by direction to certain changes to Royal Mail's Costing Manual under Acc 1.16 of the Initial Conditions in accordance with Section 53 of, and Paragraph 4 of Schedule 6 to, the Postal Services Act 2011

PROPOSAL

1. Ofcom hereby proposes, in accordance with section 53 of, and paragraph 4 of Schedule 6 to, the Act to give its consent by direction in writing to certain proposed changes to Royal Mail's Costing Manual.
2. The proposed consent by direction is set out in the Schedule hereto.
3. The effect of, and Ofcom's reasons for making, this proposal are set out in the accompanying consultation document.

OFCOM'S DUTIES AND LEGAL TESTS

4. Ofcom is satisfied that this proposal satisfies the general test in paragraph 4(2) of Schedule 6 to the Act.
5. In making this proposal, Ofcom has considered and acted in accordance with its principal duty in section 29 of the Act and its general duties in section 3 of the Communications Act 2003.

MAKING REPRESENTATIONS

6. Representations may be made to Ofcom about the proposal set out in this Notification by no later than 18 May 2012.
7. Copies of this Notification and the accompanying consultation document have been sent to the Secretary of State in accordance with paragraph 5(1) (a) of Schedule 6 to the Act.
8. By virtue of paragraph 4(8) of Schedule 6 to the Act, Ofcom may give effect, with or without modifications, to a proposal with respect to which it has published a notification only if Ofcom has—
 - (a) considered every representation about the proposal that is made to Ofcom within the period specified in this Notification; and
 - (b) had regard to every international obligation of the United Kingdom (if any) which has been notified to Ofcom for this purpose by the Secretary of State.

INTERPRETATION

9. Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them in this Notification and otherwise any word or expression shall have the same meaning as it has been ascribed for the purpose of Part 3 of the Act.

10. In this Notification—

- (a) “Act” means the Postal Services Act 2011 (c.5);
- (b) “Costing Manual” means the document produced by the universal service provider pursuant to Initial Condition Acc 1.3;
- (c) “Initial Conditions” means the conditions made pursuant to Section 66 and Schedule 9, paragraph 4-6 of the Act and set out in Ofcom’s statement of 29 September 2011;
- (d) “Ofcom” means the Office of Communications; and
- (e) “Royal Mail” means Royal Mail Group Ltd, whose registered company number in England and Wales is 04138203

11. For the purpose of interpreting this Notification—

- (a) headings and titles shall be disregarded;
- (b) expressions cognate with those referred to in this Notification shall be construed accordingly;
- (c) the Interpretation Act 1978 (c. 30) shall apply as if this Notification were an Act of Parliament.

12. The Schedule to this Notification shall form part of this Notification.

Signed by David Brown

Director of Competition Finance

A person duly authorised by Ofcom under paragraph 18 of the Schedule to the Office of Communications 2002

18 April 2012

SCHEDULE

Proposed consent by direction under Acc 1.16 of the Initial Conditions

BACKGROUND

- (A) By notification of 29 September 2011 and pursuant to Section 66 and Schedule 9, paragraph 4-6 of the Act, Ofcom imposed certain regulatory conditions (the "Initial Conditions") and directions on postal operators;
- (B) On 29 September 2011 and pursuant to Section 66 and Schedule 9, paragraph 3 of the Act, Ofcom also designated Royal Mail as the universal service provider;
- (C) Under the Initial Conditions, the universal service provider is required to maintain a Costing Manual, which may be modified in accordance with the procedure set out in the Initial Conditions;
- (D) On 18 April 2012, Ofcom issued a notification pursuant to Acc 1.16 of the Initial Conditions setting out their proposals for a consent by direction to certain changes to Royal Mail's Costing Manual;
- (E) A copy of the notification was sent to the Secretary of State in accordance with Paragraph 5(1) of Schedule 6 to the Act;
- (F) Ofcom invited representations about its proposals by 18 May 2012;
- (G) By virtue of Paragraph 4(8) of Schedule 6 to the Act, Ofcom may give effect, with or without modifications, to a proposal with respect to which a notification has been given only if Ofcom-
 - a. Has considered every representation about the proposal that is made to the person within the period specified in the notification; and
 - b. Has had regard to every international obligation of the United Kingdom (if any) which has been notified to Ofcom for the purposes of this paragraph by the Secretary of State.
- (H) Ofcom received responses to the notification and have considered every such representation made to them in respect of the proposals set out in the notification and the accompanying explanatory statement; and the Secretary of State has not notified Ofcom of any international obligation of the United Kingdom for this purpose.

DECISION

- (1) Ofcom hereby gives its consent by direction on writing, in accordance with Acc 1.16 of the Initial Conditions, as follows:
 - 1. The accommodation costs for shared space within the bulk mail processing units are to be attributed to all the products processed within the bulk mail processing units,

based on the actual accommodation costs that the processing of these products utilises by using a detailed analysis of the actual space utilised;

2. The costs associated with the mail handling equipment activity will be attributed to the products processed within the bulk mail processing units based on the actual accommodation costs that each of the products utilises;
 3. The activity recording, primarily, the cost of staff uniforms will be allocated to the 'support' process;
 4. The activity recording the costs of the 'sameday' service will be allocated to the 'Royal Mail specialist service' process;
 5. The activity recording the consolidation and segregation of bulk mail will be allocated to the 'inward mail centre' process.
- (2) The effect of, and the reasons for making this decision are set out in the explanatory statement.

OFCOM'S DUTIES AND LEGAL TESTS

- (3) Ofcom are satisfied that this consent by direction satisfies the test in paragraph 4(2) of Schedule 6 of the Act, namely that the direction is objectively justifiable, does not discriminate unduly against particular persons or a particular description of persons, is proportionate to what it is intended to achieve, and is transparent in relation to what it is intended to achieve. In giving this consent by direction, Ofcom have considered and acted in accordance with their principal duty in section 29 of the Act and their general duties in section 3 of the Communications Act.

INTERPRETATION

- (4) Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them in this Notification and otherwise any word or expression shall have the same meaning as it has been ascribed for the purpose of Part 3 of the Act.
- (5) For the purpose of interpreting this consent by direction, the following definitions shall apply:
- (a) "Act" means the Postal Services Act 2011 (c.5);
 - (b) "Costing Manual" means the document produced by the universal service provider pursuant to Initial Condition Acc 1.3;
 - (c) "Ofcom" means the Office of Communications; and
 - (d) "Royal Mail" means Royal Mail Group Ltd, whose registered company number in England and Wales is 04138203.
- (6) For the purpose of interpreting this Notification:

- (a) headings and titles shall be disregarded;
- (b) expressions cognate with those referred to in this Notification shall be construed accordingly;
- (c) the Interpretation Act 1978 (c. 30) shall apply as if this Notification were an Act of Parliament.

(7) This direction shall take effect on the date it is published.

Signed by [...]

[title]

A person duly authorised by Ofcom under paragraph 18 of the Schedule to the Office of Communications 2002

[date]