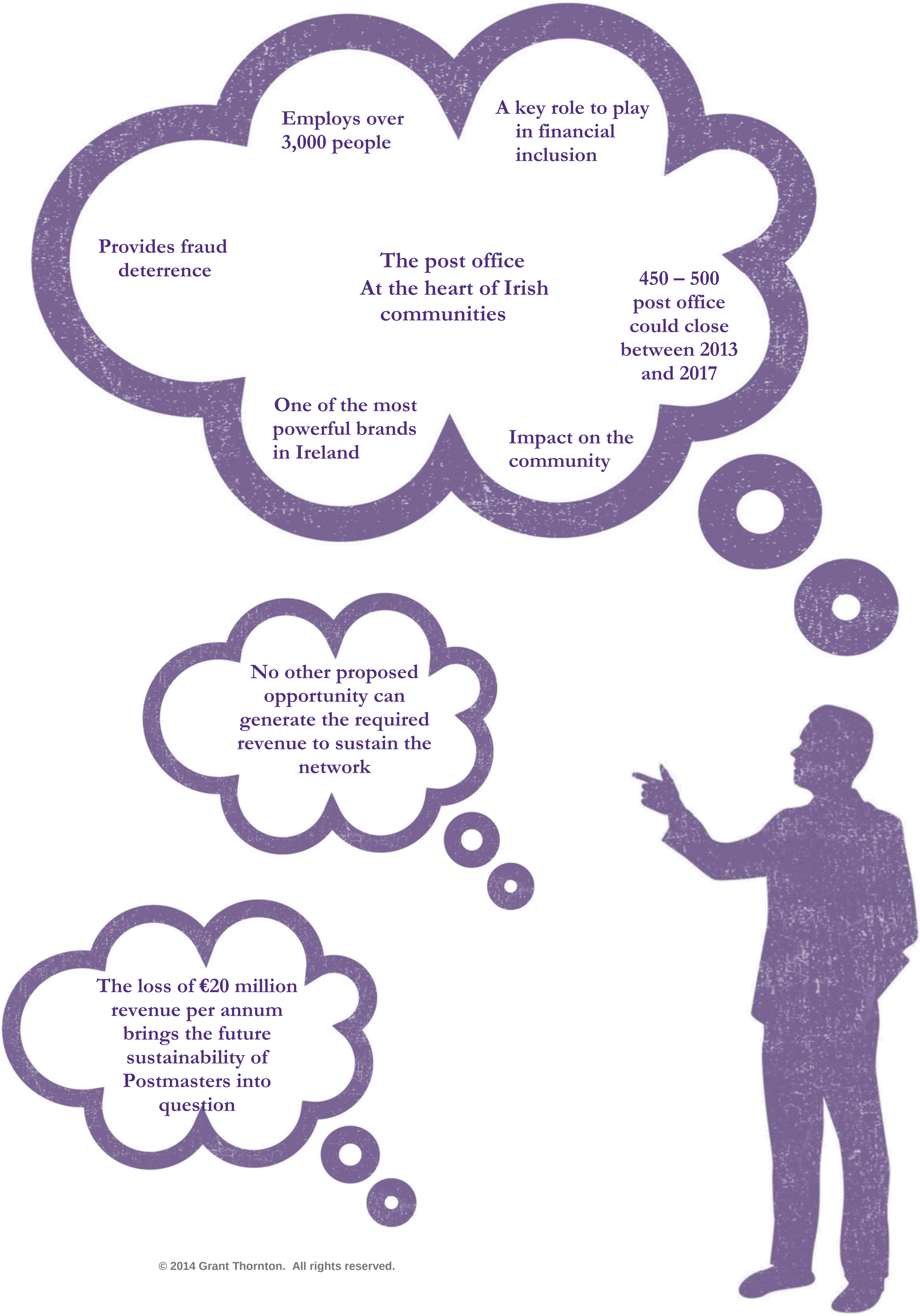
Grant Thornton
An instinct for growth™

Into the future

An assessment of the Irish post office network

February 2014

Contents


Employs over 3,000 people
A key role to play in financial inclusion
Provides fraud deterrence
The post office At the heart of Irish communities
450 – 500 post office could close between 2013 and 2017
One of the most powerful brands in Ireland
Impact on the community
No other proposed opportunity can generate the required revenue to sustain the network
The loss of €20 million revenue per annum brings the future sustainability of Postmasters into question

List of abbreviations

AIB – Allied Irish Bank

AEI – Application Enrolment Identification

BOI – Bank of Ireland

BPA – Basic Payment Account

CBA – Cost Benefit Analysis

DSP – Department of Social Protection

DWP – Department of Work and Pensions UK

EFT – Electronic Funds Transfer

IPU – Irish Postmasters Union

LPT – Local Property Tax

NFSP – National Federation of Sub Postmasters

NPV – Net Present Value

NTMA – National Treasury Management Agency

OTC – Over the Counter

POCA – Post Office Card Account

ReBo – Credit Union Restructuring Board

SBA – Standard Bank Account

SME – Small and Medium Enterprises

SW – Social Welfare

Executive Summary

Introduction

The Irish post office network (the network) is an intrinsic component of community life in Ireland but its future sustainability is under threat.

The network is dependent on the revenue it generates from two main government contracts:

- Social Welfare; and
- National Treasury Management Agency (NTMA) savings.

The contract to deliver social welfare payments through the network currently costs the exchequer in the region of €60 million per annum. Of this €60 million, the network receives €20 million per annum; this is critical income to the post office network and represents 30% of its annual revenue. The network is facing the imminent loss of the welfare contract as government pursues a policy of direct electronic payments of social welfare. In addition to the proposed loss of the welfare contract, the NTMA contract is due for renewal in 2014.

Without the revenue generated by these contracts, the network cannot survive. Currently these two contracts contribute 60% of the networks revenue. Business opportunities, capable of providing enough revenue to the network, to substitute for the loss of these contracts, do not exist.

The network is a key element of the government's financial inclusion strategy. Any weakening of the network would dilute the role it can play in helping attain greater financial inclusion. It's likely that financial exclusion may increase when the trend of bank branch closures and the percentage of the population without access to the internet are accounted for, so the role of the network is more vital than ever.

Currently, the network via it's over the counter (OTC) delivery of welfare performs an important fraud deterrent role for the Department of Social Protection (DSP). The face to face nature of the process acts as a fraud deterrent and allows for payments to be stopped at a local level with immediate effect. Uncollected payments are returned to the DSP, this accumulates to a substantial sum on an annual basis. Direct electronic payment cannot realise these fraud savings.

The proposed change to direct electronic payment of social welfare needs to be backed up by a robust cost analysis. Would this method be any more cost effective than the current OTC delivery method? This integral question currently remains unanswered.

To secure the network into the future, Grant Thornton believes government must:

- re-examine its pursuit of direct electronic payments; or
- deliver revenue of €60 million per annum to An Post (with €20 million going directly to the network) from an alternative source.

Background

In 2012, the Irish Postmasters Union (IPU) commissioned Grant Thornton to write a report on the future of the network in Ireland. The objective of the report, was to provide an assessment of the state of the network, to evaluate potential options available to it and to ensure its future sustainability.

The IPU has commissioned Grant Thornton to create a follow up report, which builds on the findings of the previous report. In particular this report underlines the detrimental impact that the loss of the social welfare contract would have on the network and the communities it serves.

Irish Postmasters Union (IPU)

An Post is the semi state body responsible for the delivery of postal services throughout Ireland. The IPU is the representative body for postmasters in Ireland. The IPU represents 90% of all postmasters.

The network

In 2012, the network employed over 3,000 employees and consisted of 1,152 post offices located throughout Ireland.

Table 0.1 – Number of post office and sub post offices

	2006	2007	2008	2009	2010	2011	2012
Company post offices	84	74	61	57	57	57	**57**
Sub-post offices	1,277	1,212	1,187	1, 179	1,107	1,099	**1,095**
Total	**1,361**	**1,286**	**1,248**	**1,236**	**1,164**	**1,156**	**1,152**

57 post offices are owned and operated by An Post and are known as company post offices. The remaining 1,095 post offices are owned and managed by independent self-employed retailers, acting as a distribution facility for An Post.

Table 0.1 highlights the decline occurring in the post office network across the years 2006 to 2012. In this period the network has seen a 15% decline, a weakening financial position further threatens the network. Revenue from traditional mail continues to decrease, while retail revenues remain overwhelmingly reliant on social welfare and savings in the NTMA, both items relating to government contracts due to expire.

Table 0.2 – An Post: revenue 2007 - 2012

	2007 €'000	2008 €'000	2009 €'000	2010 €'000	2011 €'000	2012 €'000	% Change
Republic of Ireland							
Postage: Letters & parcels	631,820	624,820	565,640	552,366	507,306	501,450	-21%
Postage: Elections and referendum	14,686	4,708	15,494	0	27,996	3,725	-75%
Post offices: Agency, remittance and related services	154,321	156,407	163,950	171,438	171,613	169,041	10%
Other services	29,042	18,547	19,783	36,197	41,598	42,072	45%
Interest income	19,192	21,622	12,890	9,259	9,358	8,760	-54%
	849,061	**826,104**	**777,757**	**769,260**	**757,871**	**725,048**	-15%
United Kingdom							
Other services	23,939	23,939	26,459	35,860	48,843	82,247	244%
Turnover	**873,000**	**850,043**	**804,216**	**805,120**	**806,714**	**807,295**	-8%

The loss of the social welfare contract would mean an immediate €60 million a year decline in the revenue of An Post with a direct loss of €20 million to the network. This revenue decline is likely to be further exacerbated by decreased footfall as a result of these changes.

Options explored in seeking to increase business for the network include:
- the network evolving into a front office for government services; and
- the provision of a greater range of financial services (e.g. banking) via the network.

These opportunities cannot realise enough revenue for the network to bridge the financial gap caused by the loss of the welfare or NTMA contracts.

Should this projected €60 million a year deficit not be bridged then widespread post office closures would follow. Such a repercussion raises concerns not just for the network, but for the communities and citizens the network serves.

Strategic context

Since our prior year report, a number of developments, likely to have an impact on the network have taken place. These developments relate to events in the macroeconomic, public and financial service sectors.

In a significant change to the existing contract, the future welfare contract is split into two parts:

1 the provision of OTC social welfare payments service; and

2 the provision of an e-payment solution to replace the existing facility to make payments directly into customer's accounts.[1]

An Post has retained the OTC contract for at least 2 more years until December 2015, with a possibility to extend the contract for up to 4 years.

The procurement for the second contract was due to commence in late 2013 but this has now been deferred by the Minister for Social Protection. The DSP aims to have three quarters of all social

[1] http://www.kildarestreet.com/wrans/?id=2013-05-21a.901

welfare payments paid into accounts in financial institutions or prepaid cards or via mobile phones by 2017.[2]

The medium and long term implications of the DSP strategy form the basis of the Grant Thornton's concern over the networks future sustainability.

Case study: the UK experience

The UK experience with direct electronic payments should be analysed by government before proceeding further.

The main lessons that the Irish government can take from the UK experience are as follows:

- government must act to bridge the potential €60 million a year deficit, facing the network or it cannot survive; and
- if continuing with its direct electronic payments policy, government should:
  - design a model of direct electronic payments that meets the needs of both the DSP and the network;
  - allow for the creation of an exceptions list, so the public can opt out of electronic fund transfers and continue receiving welfare payments OTC;
  - conduct an impact assessment, to understand the loss the network would have for Irish communities both economically and socially; and
  - explore subvention.

Post office closures have a negative economic impact for the wider community as highlighted in the Devon case study. This study also articulates the detrimental impact closures can have on older and more vulnerable members of the community.

Financial inclusion

Financial inclusion relates to the delivery of financial services at affordable cost to all sections of society, in particular the disadvantaged and those on low income.

There is a high correlation between low income and financial exclusion, and it is likely that the majority of those financially excluded are in receipt of welfare. Levels of financial exclusion are significantly higher in Ireland than in other European Union countries. A lack of trust in the banking system has also contributed to some people electing to remain outside of the financial system.

In addressing the issue of financial exclusion the government's 'Strategy for Financial Inclusion', identifies the provision of a Basic Payment Account (BPA), as a logical first step. A BPA is a transaction account designed to meet the needs of the financially excluded. Regular use of a BPA would mean that the account holder builds up a financial profile. This could enhance their creditworthiness for providers of mainstream credit.

The strategy for financial inclusion identifies the network as having a key role to play in the provision of a BPA. "It should be noted that the role of the post office as an access point to the BPA will have an important part to play in ensuring the sustainability of the post office network".

---

[2] http://www.independent.ie/irish-news/cash-payments-for-social-welfare-claimants-to-be-phased-out-by-2017-29246493.html

Grant Thornton would stress that government needs to undertake a detailed costing of any proposed BPA, and identify what party would bear the cost of the provision of such a service. If the proposed BPA is to be used as a destination for the Electronic Fund Transfer (EFT) of social welfare payments then it needs to be clarified if such an approach is any way more cost effective than the current OTC delivery.

If the deficit facing the network is not addressed, it cannot survive to play its part in achieving financial inclusion. If the network is not involved in the provision of the BPA, then those living in the increasing number of communities throughout the country without access to financial services would find themselves financially excluded.

Fraud

The roll out of social welfare cards and the recent creation of a fraud control panel underline the government's commitment to clamp down on welfare fraud.

The network, through its OTC delivery of the welfare contract provides a number of effective measures that can help reduce fraud. The transition to a system of direct electronic payments would mean these mechanisms of fraud reduction are eliminated.

Currently, the network can withhold payment at an individual level. This effective mechanism allows the network to work with the DSP in managing fraud at a local level. The system of direct electronic payments would remove such measures.

The network also returns to the DSP, substantial sums of money in uncollected payments. The proposed direct electronic payments method of welfare delivery removes this mechanism, and uncollected payments may go undetected and there would be no refund to the exchequer.

Loss of the Social Welfare Contract

To better understand the potential implications the loss of the welfare contract would have for the network, this report examines three possible scenarios:

- scenario 1 – No change – social welfare contract renewed and e-payment strategy doesn't go ahead;
- scenario 2 – Social welfare contract lost – complete loss of revenues; and
- scenario 3 – Social welfare contract renewed but at a lower level of transactions due to the move to e-payment.

The findings highlight the stark reality the loss of the social welfare contract could have for the network as outlined in the table below.

Table 0.3 – Projected network size

Network size	2012	2017	Office Closures	% Change
Scenario 1	1,150	1,042	8	-9%
Scenario 2	1,150	593	557	-48%
Scenario 3	1,150	706	444	-39%

Source: Grant Thornton analysis

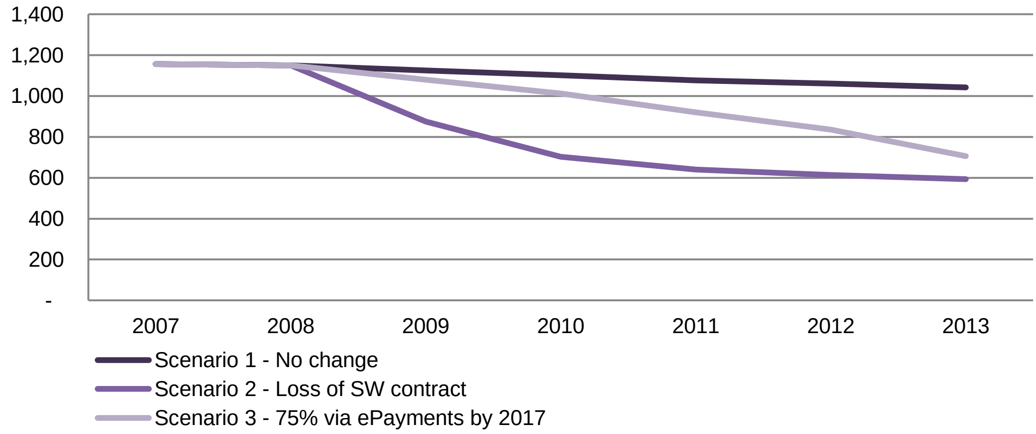
If as per scenario 3 the welfare contract is renewed but with fewer transactions due to the move to e-payment, then the network cannot survive. The shortfall in funding, that scenario 3 creates would need to be addressed either by subvention or an alternative method.

The provision by the network of further financial services and its expansion into a front office for government services could generate much needed additional revenue. However the revenue generated from these measures alone would not be enough to secure the network in its current state.

Summary of findings

An Post is faced with a €60 million per annum financial deficit as a result of the loss of the welfare contract with €20 million being directly lost by the network. Unless action is taken to secure the networks sustainability, the consequences to the network and the wider communities it serves would be drastic.

Figure 0.1 Post office numbers – various scenarios



Options to increase and expand the services offered by the network (financial and government front office) have been explored, but the revenues that could be generated as a result would not alone be sufficient in substituting for the loss of the social welfare contract.

Despite continued assertions by government officials as to the importance of the network, little support is being offered to it. Government must take action now to safeguard the future of the network and in doing so, protect and retain access to services at a community level.

Grant Thornton would recommend government to pause and consider the following:

- the inadvertent contribution to financial exclusion;
- fraud risk, and loss of control associated with EFT payments; and
- the impact on citizens and communities if the network is left to deteriorate.

For the network to be sustainable into the future it requires action by government now. The transfer of additional government front office services including motor tax and the increasing of financial services offered by the network are the two most viable options identified to help sustain the network.

Conclusion

The imminent loss of the social welfare contract has serious repercussions for the network, and the wider community it serves.

Government, aware of the unique role the network plays in Irish communities must act now if it is to secure the network into the future.

The primary reasons for government action are:

- the fraud deterrence's performed by the network, including refunds to the DSP in relation to uncollected welfare payments cannot be replicated in a direct electronic payments model;
- the inadvertent contribution that the decline of the network would have in increasing financial exclusion;
- the negative economic impact of post office closures on communities;
- the intrinsic and unquantifiable role played by the network in Irish communities; and
- the network employs over 3,000 people.

The most viable of options to secure the network is for government to maintain its existing contracts with it. For the network to survive, the revenue the welfare contract generates would need to be retained or replaced.

Adopting a model of direct electronic payments that does not destabilise the network and encouraging the use of an exceptions list would help secure the networks future.

The provision by the network of further financial services and its expansion into a front office for government services could generate much needed additional revenue. However the revenue generated from these measures alone would not be enough to secure the network in its current state. Table 0.4 overleaf provides an overview of the key findings of the report.

Table 0.4 – Key findings

Key Findings

• the networks future sustainability is at risk owing to changes in government contracts due for renewal. The contracts in question are:
  • the social welfare contract; and
  • NTMA savings.

• the social welfare contract is worth €60million per annum to An Post with €20 million of this accruing directly to the network. The network cannot survive without maintaining its current revenue.
• options to expand the financial services and the evolution into a front office for government services are critical to the network. However these alone would not deliver sufficient revenue to sustain the network when accounting for the loss of the welfare contract.
• learn from the UK experience where a move to direct electronic payments of welfare and failure by government to deliver additional services and business for the network has contributed to its decline.

• Before embarking on a system of direct electronic payments Grant Thornton would call on the government to consider:
  • the cost savings direct electronic payments has over the current OTC method;
  • the inadvertent contribution direct electronic payments would have to financial exclusion;
  • fraud risk, and loss of control associated with EFT payments; and
  • the impact on citizens and communities including the economic consequences for the community if the network is left to deteriorate

Before introducing a BPA it needs to be established if this method of service delivery is any way more cost efficient than OTC payments The party that would bear the cost of the BPA also needs to be identified. A model for the introduction of the BPA and the move to EFT social welfare payments is explored below:
• identify who would bear the cost of the BPA, and
• clarify if this could be any more cost effective than the current OTC service delivery mode;
• if proceeding with the introduction of a BPA:
  • BPA should be made available through the post office network, and be the sole source of social welfare payments;
  • the default option being a direct electronic payments via EFT into a BPA; and
  • include an opt out clause that allows for the continuation of OTC services for welfare payment.

• scenario 1, if there is no change to existing government contracts and network revenues remain stagnant then the number of post offices would decline from 1,150 at present to 1,042 by 2017; • scenario 2, if the network loses the social welfare contract only 593 post offices may remain in 2017, representing a decline in network size of 48%; and • scenario 3, if direct electronic payments is introduced and 75% of payments occur via EFT without the involvement of the network, with the remainder delivered via OTC by the network then only 706 post offices may remain by 2017, representing a decline in network size of 39%.
• to sustain the network government needs to act now and in so doing address the issue from the perspective of both economic and social policy.

1 Introduction

The long term sustainability of the post office network in Ireland is under threat. This threat results from the continuous revenue decline of traditional mail, and the imminent loss of two vital government contracts:

- the Social Welfare Contract; and
- NTMA savings.

The social welfare contract generates €60 million per annum for An Post with €20 million of this accruing to the network. Although NTMA savings is a financial service it can also be deemed a government contract. 60% of all network revenues are generated as a result of these two contracts and the government TV licences contract.

The loss of the social welfare contract could result in a 30% decline in network revenue. The network cannot sustain such a loss. The NTMA contract is due to be renewed in 2014 and it is vital the network retains this on a long term basis. The sustainability of the network into the future is in jeopardy without the revenue currently generated by these contracts.

Network closures would have serious implications for communities across Ireland. Failure to sustain the network could jeopardise the government's ability to deliver on its financial inclusion strategy. Government seeking to realise fraud related savings would lose out on the fraud deterrence currently provided by the network in its OTC delivery of the welfare contract.

Background to the review

In 2012 the IPU requested Grant Thornton to prepare a report on the future of the post office network in Ireland. The objective of the 2012 report was to provide an assessment of the state of the network and to evaluate potential options available to the network to ensure its future sustainability.

Key findings from the 2012 review

The 2012 report, found the financial viability of the network was under threat, owing to a decline in the traditional revenue base and also due to a high dependence on the contract to deliver social welfare payments. Opportunities were identified that could be added to the networks offering to ensure its future sustainability.

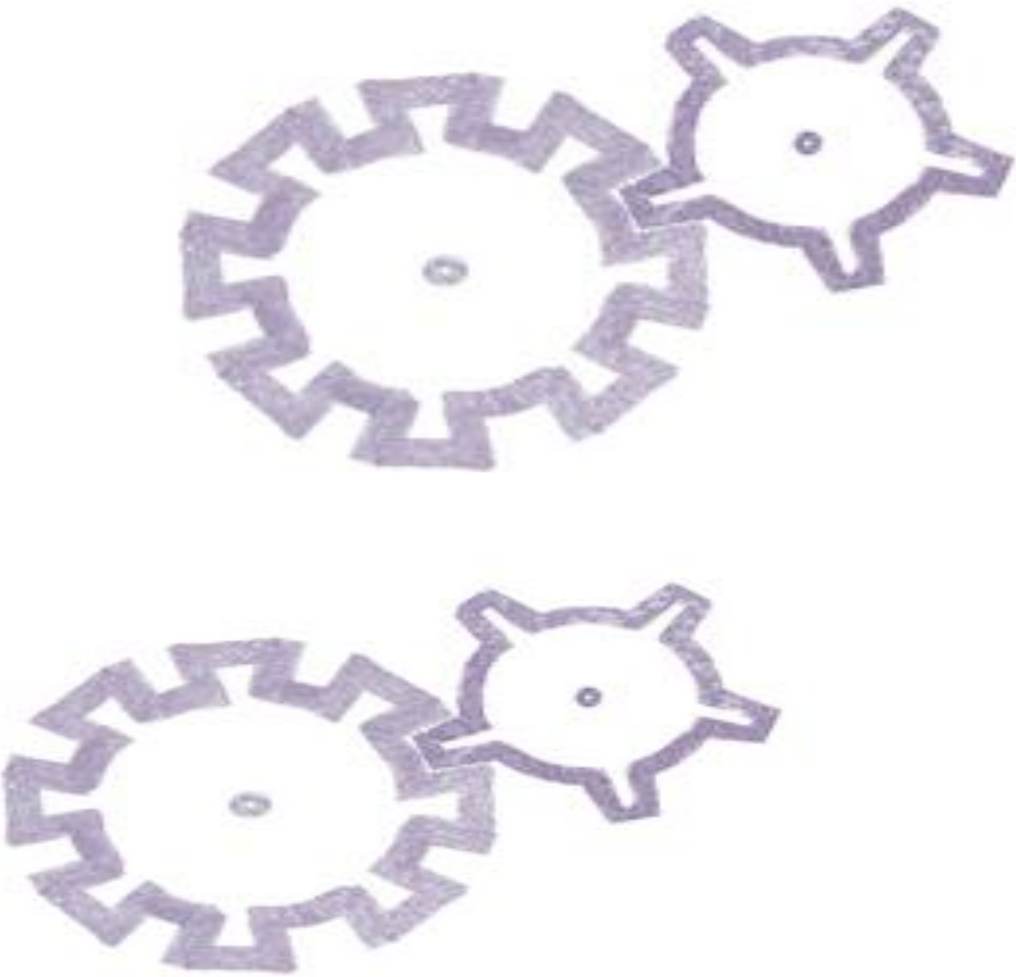
These were:

- the provision of OTC motor tax renewals;
- an extension of banking services;
- payment of household charges through the network; and
- payment of hospital charges through the Billpay system.

Objective of the 2013 review

The objective of this follow up report is to:

1 reaffirm the challenges being faced by the network;
2 investigate the similarities to the UK experience;
3 identify any recent developments in the internal and external operating environment that could have an impact on the network;
4 reassess and evaluate the potential options available to the network; and
5 highlight the impact the loss of the social welfare contract would have on the network and explore possible sustainable solutions.



2 The network

This section of the report provides an overview of the network and recaps on some of its core strengths and weaknesses.

Size and makeup of the network

The network is comprised of 1,152 post offices across Ireland. Of these 1,152 post offices, 57 are owned and operated by An Post (company post offices), and 1,095 sub-post offices are owned and managed by independent self-employed postmasters.

Table 2.1 – Number of post offices and sub post offices

	2006	2007	2008	2009	2010	2011	2012
Company post offices	84	74	61	57	57	57	**57**
Sub-post offices	1,277	1,212	1,187	1, 179	1,107	1,099	**1,095**
Total	**1,361**	**1,286**	**1,248**	**1,236**	**1,164**	**1,156**	**1,152**

Products and services

The 1,152 post offices offer a great diversity of products and services. These products and services are outlined in the table below.

Table 2.2 – post office products and services

Personal		Business	
Mail	Sending Mail Passport Express Registered Post International International Courier Service Express Post International Courier Post Redelivery Redirection MailMinder	**Mail**	Sending Mail Registered Post National Standard Post eDocketing Buy stamps Meter - Franking Discount For Volume Mailers Business Response - Freepost Business Redirection
Pay	Pay bills TV Licence Property tax Dog Licence Garda Fixed Fines Tolltag.ie	**Marketing**	Mail Media website Products and Services Publicity Post PostAim Admailer.ie Tools and Guides Case studies Research, trends and insights
Do More	Buy Dollars or Sterling Transfer money Insurance Postbreaks Gift Vouchers	**Do more**	Easy Post Stamp Printer Speed up your post Sending mail tips Bulk Mail Publication services TV Licence

Personal		Business	
Financial	State Savings & Investments National Solidarity Bond Prize Bonds; No charge Personal savings accounts Banking at the post office	**Parcels**	Sending Parcels 30+ Parcels a week Importing or Exporting e-Commerce experts

One of the key findings from our previous report was that the network needed product offerings alone such as motor taxation, more banking services and other government front office services.

This report again calls for such action; however, it should be noted these additional service offerings would not generate sufficient revenues to compensate for the loss of the social welfare contract. Additional products and services would contribute to but not secure the networks sustainability into the future.

Joint Oireachtas Committee

In March 2013, the Joint Oireachtas Committee on transport and communications published a report on promoting a sustainable future for the network. The report highlights the vital role played by the network in rural and urban communities across Ireland. Consistent with Grant Thornton's 2012 report the Oireachtas committee report identifies the potential loss of the social welfare contract as having serious implications for the networks sustainable future. The report also outlines the important social service the network provides and makes several recommendations in relation to securing the future sustainability of the network.

Capacity and capability

The network remains in a strong position to add additional services. The majority of postmasters have available capacity should additional services be added and the IT system (Riposte) has the capability to facilitate this if so required.[3]

Brand/reputation

The network remains among one of the most powerful brands in Ireland. This fact has been recognised in the RepTrak survey which named An Post as "the most reputable indigenous Irish firm" for the third year in a row.

Key financial indicators

Though it was not possible to consolidate the financial information of individual post offices, we can draw sufficient conclusions from the An Post annual report. This report provides the required information to identify trends and analyse the performance of the network.

Over a five year period revenues have fallen by 8%. The reduction in revenues for the network is actually greater as income for An Post has been supplemented by a growth in income from the UK, which is irrelevant to the Irish network.

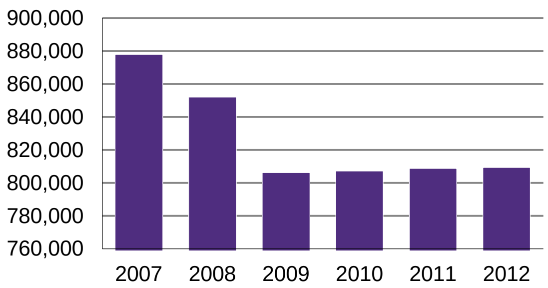
Table 2.3 shows income from the network was down 15% when UK revenues are excluded. This decrease was largely driven by the fall in demand for traditional mail, which has reduced from €631k to €501k, in the period 2007 to 2012, a fall of 21%.

[3] IPU Members Survey 2011

Table 2.3 – An Post revenue (2007 – 2012)

	2007 €'000	2008 €'000	2009 €'000	2010 €'000	2011 €'000	2012 €'000	Overall % Change
Republic of Ireland							
Postage: Letters & parcels	631,820	624,820	565,640	552,366	507,306	501,450	-21%
Postage: Elections and referendum	14,686	4,708	15,494	0	27,996	3,725	-75%
Post offices: Agency, remittance and related services	154,321	156,407	163,950	171,438	171,613	169,041	10%
Other services	29,042	18,547	19,783	36,197	41,598	42,072	45%
Interest income	19,192	21,622	12,890	9,259	9,358	8,760	-54%
	849,061	**826,104**	**777,757**	**769,260**	**757,871**	**725,048**	-15%
United Kingdom							
Other services	23,939	23,939	26,459	35,860	48,843	82,247	244%
Turnover	**873,000**	**850,043**	**804,216**	**805,120**	**806,714**	**807,295**	-8%

Figure 2.1 - An Post Revenue (2007 -2012)



Retail revenues declined marginally from 2011 but they continue to perform strongly at €169 million, which represents an increase of 10% from 2007.

Retail revenue is dominated by income from two government contracts:

1 social welfare payments; and
2 savings in the NTMA.

These two contracts represent 60% of total retail income. The dependence on these two contracts is a concern for the network. This dependence is most pronounced in smaller and medium sub-post offices. There is no contract in the pipeline that could replace the revenue generated by either of these existing contracts. The loss of revenue associated with the loss of one or both of these contracts would result in network closures.

Table 2.4 – Revenue breakdown by post office size and source

Office Type	Mails	DSP	Billpay	Savings	Money Transfer	Other
An Post	27%	34%	15%	10%	3%	11%
Sub-post office large	27%	34%	20%	9%	2%	8%
Sub-post office medium	31%	32%	16%	11%	3%	7%
Sub-post office small	28%	37%	13%	12%	3%	7%

Findings from prior year review

The 2012 report identified the core strengths and weaknesses of the network. The weaknesses identified present a challenge to the long term sustainability of the network. Most significant amongst these weaknesses is the dependence on the social welfare contract.

Figure 2.5 – Strengths and weaknesses of the network

Strengths	Weaknesses
– Social welfare fraud deterrent - face to face contact; – Irelands largest retail network with over 1,100 post offices in Ireland; – Brand: Household name with positive customer perception; – Social welfare contract (a threat and a weakness); – Large customer base; – Goodwill - customer trust; – Proven track record of service delivery; – Ability to handle large volumes; – Community and social centre; – Communication structure; – Low levels of gearing (debt); – Flexible systems with the ability to add services (Riposte System); – Capacity to handle additional business; and – Local knowledge and customer knowledge.	– Dependence on government contracts incl (social welfare and NTMA savings); – Idle time (certain offices); – Inconsistent service offerings; – Varied financial performance; – Supplier power; – Restrictions on marketing; – Structure – inherent difficulty of independent entities with standardised product offering; – Identity - different view of own role (Postmasters); and – Pay scale is complex and not fully understood.

Conclusions

Since the previous year's report, the financial sustainability of the network remains under threat. Revenue from traditional mail continues to decrease whilst retail revenues remain largely reliant on social welfare payments and the NTMA contract.

The proposed extension of the products and services offered by the network to include motor taxation and other government front office services has not taken place. It should be noted these additional service offerings would not generate sufficient revenues to compensate for the loss of the social welfare contract. Additional products and services would contribute to but not secure the networks sustainability into the future.

Without action the network risks becoming unsustainable, any post office closures would have a negative impact on the economic and social life of many communities across Ireland.

3 Strategic context

In this section we outline developments that impact the strategic environment of the network and highlight the possible implications these developments may have on its future sustainability.

The key focus will be on three core areas:

- macro-economic;
- Public sector (including local government); and
- the financial services sector.

Macro-economic

The on-going economic situation creates a challenging business environment for the network. The economic downturn and high level of unemployment have a twofold impact on post office business. On the one hand, the amount of recipients of social welfare payment through the post office remains high; whilst on the other hand; low levels of disposable income have impacted negatively on retail sales.

Public sector

The public service reform plan and changes in respect of the delivery of social welfare payments both have implications for the network.

The Public Service Reform Plan

The Public Sector Reform Plan, published in 2011, forms the basis for current and upcoming changes in the public sector.

The implications of this plan on the network are:

- the future emphasis on innovative service delivery channels, such as the internet, consequently creates a requirement for OTC service for those unable or unwilling to access same;
- the post office has the capacity and nationwide reach to provide this service;
- the amalgamation of a number of county councils and introduction of municipal districts may limit the ability of the public to access government services and as such create a role for the network to evolve into a government front office; and
- the migration of government services to the network would enable government (local and national) to redeploy resources and realise savings elsewhere.

Delivery of social welfare payments

A significant change to the existing contract is that the future contract is to be split into two separate parts:

- the provision of OTC social welfare payments service; and

- the provision of an e-Payment solution to replace the existing facility to make payments directly into customer's accounts.[4]

For the first contract, An Post has been selected as the preferential bidder. As a result, An Post has retained the contract for at least 2 more years until December 2015 with the possibility to extend the contract for up to 6 years. This is helpful in sustaining the network in the short term.

The procurement for the second contract was due to commence in late 2013 but this has now been deferred. The DSP aims to have three quarters of all the social welfare payments paid into accounts in financial institutions or prepaid cards or via mobile phones by 2017.[5]

The medium and long term implications of this strategy would have negative impacts for the network.

Local property tax

The introduction of the temporary household charge in 2012 and the subsequent local property tax (LPT) in July 2013 have been one of the largest reforms in local government financing since the foundation of the State. [6]

One of the primary reasons advanced for the initial poor compliance, was the limited range of payment options available to homeowners. At the time of writing this report, the revenue commissioners estimate that 89% of the estimated 1.96 million properties that are liable for the charge have complied with it. [7] Had the government engaged with community based stakeholders, the compliance rate could have been much higher.

Since the new local property tax was introduced in July 2013 homeowners can now pay their property tax at their local post office. To facilitate this service a Tax-Pay service of €1 per transaction is applied by An Post.

Croke Park Agreement and Haddington Road Agreements

The Croke Park agreement was recently revised to include additional clauses and new provisions for public sector employees.

The most important part of the agreement, to be taken into account when devising a future strategy for the post office, is concerned with the redeployment of public servants.

Public bodies are under pressure to seek more efficient service delivery channels and aim to maximise the use of online facilities.

This creates an opportunity for the post office to be the front office for government service delivery (motor taxation and other options, explored further in this document). This would allow the government to distribute scarce human resources in a more effective way. Such a development would also allow for the continuation of OTC services to those without access or technical ability to execute digital transactions.

---

[4] http://www.kildarestreet.com/wrans/?id=2013-05-21a.901
[5] http://www.independent.ie/irish-news/cash-payments-for-social-welfare-claimants-to-be-phased-out-by-2017-29246493.html
[6] http://www.environ.ie/en/Environment/News/MainBody,28846,en.htmn
[7] http://www.revenue.ie/en/press/2013/pr-240713-lpt.html

Motor tax

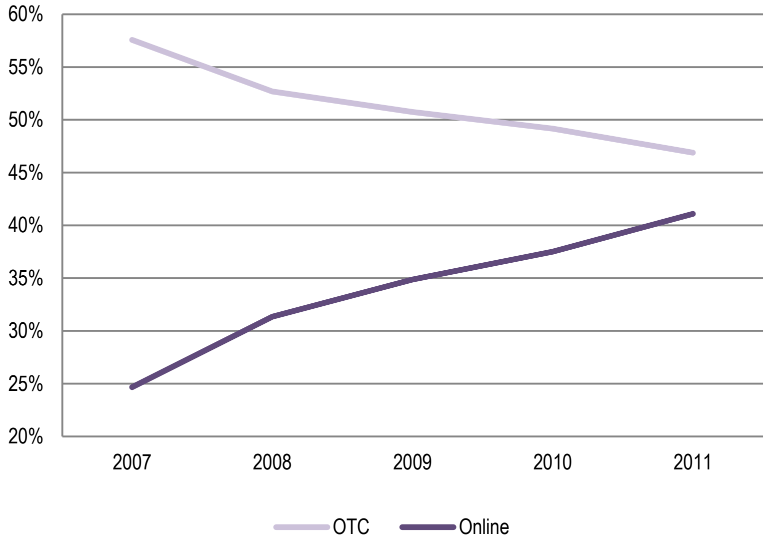
The most recent statistics published by the Department of the Environment, Community and Local Government shows that OTC payments continue to be the primary method of paying for motor tax in Ireland.

Table 3.1 – Motor tax receipts by type

	2007	2008	2009	2010	2011
OTC	58%	53%	51%	49%	47%
Online	25%	31%	35%	38%	41%
Post	18%	16%	14%	13%	12%

Source: Annual report, Department of Environment, Community and Local Government 2012

Figure 3.1 – Motor tax transactions by type



Source: Department of Environment and Local Government, Service indicators in LA's 2007-2011

The biggest development in the area of motor tax since our previous report has been the introduction of new rules and regulations regarding declaring vehicles off the road. The new rules require owners to declare that their vehicle will not be in use prospectively at their motor tax office. Previously, the declaration could be made retrospectively at any Garda station.

It is likely that the new requirement may increase the amount of applicants at the motor tax offices. Alternatively, behaviour may change as the reduction in an incentive to seek a rebate could reduce the amount of direct applicants and drive more applications online.

Motor tax renewals have been identified as a potential addition to the networks current product and service offering. In the 2012 report, the potential Net Present Value (NPV) of additional benefit associated with motor taxation for the network was estimated at €60.6 million over a five year period.

Taking into account the requirement for public bodies to more efficiently deliver public services, as per the Croke Park and Haddington Road agreements discussed above, now could be an opportune time for the network to be asked to provide such OTC government services.

Financial services sector

An Post provides a range of financial services that currently include transactions (bill pay), foreign exchange and banking on behalf of AIB as well as Danske Bank (formerly National Irish Bank) and money transfer. Significant developments since our previous report in the financial services sector have been:

- bank branch closures;
- basic payment account pilot;
- the rise in fees associated with holding a current account;
- the introduction of the Personal Insolvency Act 2013;
- enactment of the new Credit Union Act 2012; and
- establishment of the Credit Union Restructuring Board ("ReBo").

Bank branch closures

Banks, seeking further efficiencies in the current turbulent economic environment, have moved to close several local branches:

- Ulster Bank plans to lay off as many as 1,800 staff and close up to 40 branches;[8]
- AIB has plans to close 67 branches, leaving only 200;[9] and
- Permanent TSB closed 16 branches, while it changed two into self-service branches and amalgamated two more. It has 72 full branches left.[10]

40% of the Irish population now live in areas with limited access to financial institutions.[11] The growing trend of bank branch closures mean this percentage looks set to increase and with this the risk of financial exclusion grows.

Only 78% of the Irish population have access to internet and many more lack the technical knowhow to avail of online banking services.[12] Without action many people may find themselves financially excluded.

In order to maintain the existing customer base, banks are forced to seek alternative ways to deliver their OTC services. AIB and Danske Bank provide current account and credit card services for their customers through the network. In 2012, the value of AIB transactions carried out by the network was in excess of €3 million.[13] In the context of recent closures, other banks should consider offering their services through the network. In fact in areas where AIB has closed bank branches it has transferred services to the local post office.

In addition, more opportunities for collaboration between banks and An Post should arise from the government strategy for financial inclusion. If the network declines as a result of the loss of the social welfare contract or a decline in income associated with the NTMA contract, then its role in financial inclusion would be diluted. Such a development would contribute to increasing the level of financial exclusion in society.

Basic payments account

Financial exclusion continues to be widespread in Ireland, with a number of citizens continuing to operate without access to any level of financial services.

[8] http://www.independent.ie/business/irish/ulster-bank-to-slash-branches-and-lay-off-up-to-1800-workers-29390739.html
[9] http://www.irishtimes.com/business/sectors/financial-services/aib-plans-350-million-cut-in-operating-costs-over-next-two-years-1.1363880
[10] https://www.permanenttsb.ie/about-us/news/july2012/permanent-tsb-restructuring-plan-details/
[11] CSO, accessed on 18 June 2013.
[12] http://www.comreg.ie/_fileupload/publications/ComReg1356.pdf
[13] Joint Committee on transport and communications – Report on Promoting a sustainable future for the network.

One solution proposed in the "Strategy for Financial Inclusion" released in 2011 is the introduction of a Basic Payments Account (BPA) to citizens of the state that currently do not have access to a bank account.

Whilst the banks would have to play an important role in any such strategy, the network has been mentioned as a potential partner for the government in this regard.

> *"The banks are the only financial service institutions in the State with the necessary infrastructure in place to offer a BPA at this point in time. However, as much as possible and consistent with ensuring that the strategy is implemented on a timely basis, there are other parties that have the potential to play a key role - in particular An Post."*
>
> ***- Strategy for Financial inclusion Final Report, 2011***

In June 2012, the government launched a nine month pilot Standard Bank Account (SBA) or Basic Payment Account (BPA) through three banks (AIB, Bank of Ireland and Permanent TSB) across three locations.

The results of the pilot were less than encouraging with only 205 accounts being opened, against a target of 1,000. An Post's exclusion from the pilot project had an acknowledged impact on its poor performance.

The poor performance of this pilot, suggests that only through a more aligned strategy with social welfare and the inclusion of the network can the introduction of such an account be successful.

The BPA might also act as a potential catalyst for banks to partner with the network in the delivery of a wider range of financial services.

The role the network can play in increasing financial inclusion is dependent on it retaining its size and geographic spread. The proposed loss of the social welfare contract would negatively impact on both; as a result, securing increased financial inclusion may be more challenging.

The government in seeking to address financial inclusion needs to account for the impact the loss of the social welfare contract would have on the network and its subsequent ability to play its part in financial inclusion.

Introduction of current account bank fees

Banks continue to increase current account charges making owning a bank account more expensive. Ulster Bank was the last bank to offer free banking. In July 2013, it too, introduced current account charges.

Table 3.2– Free banking requirements

Bank	Requirement
AIB	Balance of €2,500 throughout the full fee quarter
Bank of Ireland	Balance of €3,000 throughout the full fee quarter
Ulster Bank	Balance or lodgement of €3,000
Permanent TSB	Lodgement of at least €1,500

Increased competition is expected between banks for current account customers looking for the most affordable banking solution.

The network can capitalise on this opportunity and offer its clients a banking product similar to the one offered by the post office in UK.

Credit Union reform

The Credit Union is undergoing a period of reform.

The Credit Union and Co-Operation with overseas regulators act 2012 is seeking to change:

- governance requirements for Credit Unions; and
- oversight and general policy functions.

The Credit Union Restructuring Board (ReBo) was established by the Minister for Finance on 1st January 2013 to facilitate the voluntary restructuring of the Credit Union sector in accordance with the provisions of the Credit Union and Co-Operation with Overseas Regulators Act 2012.

This period of reform opens up the opportunity for talks between the network and the Credit Unions in relation to the formation of a strategic alliance that would result in the provision of credit services by the network. Whilst acknowledging the complexities involved in the creation of such an alliance, a starting point could be with larger Credit Unions. This idea is explored in further detail in section 6 of this report.

Conclusion

Since the previous report, there have been a number of significant developments in the external operating landscape that are likely to have an impact for the network.

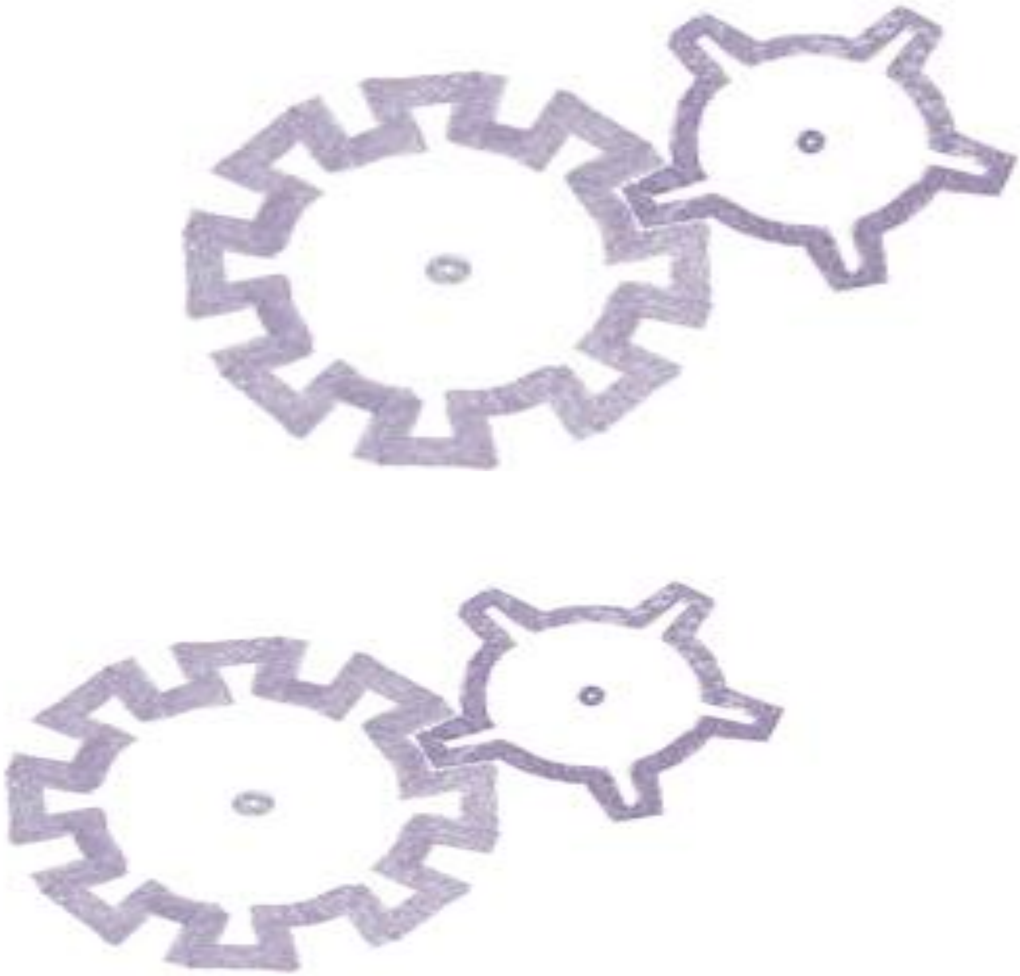
The most concerning development is the change to the social welfare contract. Should the network lose this contract its ability to play a role in increasing financial inclusion would be lessened.

Table 3.3 below summarises the developments that have occurred in the external operating landscape.

Table 3.3– Summary of recent developments

Macro-Economic context	
General	– Continued difficult operating environment – High unemployment levels persist – Continued focus on austerity
Public sector	
Public Service reform plan	– Basis for changes in public sector
Local Government	– Funding remains highly centralised – Rationalisation of city and county councils – Introduction of water charges – Introduction of property tax
Social Welfare	– Current contract for delivery of social welfare expired Dec 2013 – Procurement process has been split into two distinct pieces 1. e-Payments 2. Over the counter – An Post selected as preferred bidder for (OTC) to 2015, plus 4 – DSP aim to have 75% of social welfare paid into bank accounts by 2017
Motor Taxation	– Continued trends of move to online – Large amount remain offline (41%) – Introduction of closure to off-road loophole – Likely to save €55m

Haddington Road	– Update to Croke Park agreement
	– Increment freezes
	– Redeployment remains
Garda Stations	– Closure of 95 Garda stations
Financial services	
	– Bank branch closures
	– Introduction of bank fees
	– Introduction of personal insolvency bill
	– Establishment of ReBo
	– BPA pilot failure



4 Case Study: the UK experience

The postal market in the United Kingdom (UK) provides valuable insights into where the Irish market is going. Most importantly this benchmark analysis identifies important lessons that should be taken from the UK experience.

Research

To understand the key developments that shaped the UK market, Grant Thornton and the IPU held consultations with the National Federation of Sub Postmasters in the UK. The National Federation of Sub Postmasters (NFSP) is the national representative body that represents sub postmasters in the United Kingdom.

The UK experience

The UK and Irish postal networks are similar in nature, both have an important social focus; and both are heavily relied upon by citizens and businesses alike in both urban and rural communities.

In the UK, 4% of villages have a bank, compared to 60% which have a post office. At a time when the Irish bank branch network is contracting it is crucial that the post office network manages to retain its strength. The network is the largest of its kind in Ireland and plays an important social and economic role in communities across the country.

Between 2000 and 2013 rural areas in the UK experienced a 58.3% loss of banks and building societies (in comparison, metropolitan areas lost 15.4% banks and building societies), compared to a 35.8% loss of post offices during the same period. A similar situation to this is currently evolving in Ireland, with a large number of bank closures having occurred in the last number of years.

Direct electronic payments by the UK government saw the payment of state pensions and benefits over the post office counter replaced by electronic payments (e-Payments) made directly into an account. The scheme began in 2003 and was completed in 2005. So the comparisons and lessons to be learnt from the UK experience run deep from an Irish context.

UK Welfare Business

The programme began in 2003 and was completed in 2005, resulting in a 40% decline in traditional income for the UK network in the same period according to the NFSP.

The UK government claimed Direct electronic payments would help tackle financial exclusion and provide a cheaper method of paying pensions and benefits.

Under Direct electronic payments there were three main options for the receipt of state pensions and benefits:

1 a current or savings account at any bank or building society;
2 a basic bank account; or
3 the post office card account (POCA), which was introduced in April 2003.

An exceptions list was created from a small number of pensioners and benefit claimants who cannot manage to use electronic payment to receive their entitlements. For these individuals these cheques can be cashed at any post office or paid into bank accounts.

The revenue decline for the UK network, as a result of the Direct electronic payments scheme was drastic. The 40% decline in traditional revenues has contributed to the networks decline and this has been compounded by the failure to realise opportunities in respect of an expansion to become a front office for government services.

UK front office experience

Despite transformation programmes and subvention the UK network is continuing to decline and it is likely that there will be a compulsory closure programme in the future.

A major reason for the failure of the network transformation programmes in the UK has been the continuous erosion of services and a failure by the UK government in its commitment to deliver more front office services.

> *"We want to see the post office become a genuine front office for government at both the national and local level".*
> ***Department for Business, Innovation and Skills, National Policy Statement, November 2010***

Despite a target to provide an additional £400 million in government services through the UK network only £116 million has been delivered. The failure to supply these services has exacerbated a difficult situation and left many local post offices struggling to survive.

Potential additional revenue has been passed through the UK network as part of Application Enrolment Identification (AEI) services. These include: identity verification, identity processing (i.e. assisted applications, check and send) and payments to or from customers.

However it needs to be noted that:

- ID checking services yielded no income at all for 94% of sub-postmasters and less than £10 for the vast majority of those who do earn anything;
- 96% earn nothing from transactions available through (AEI) services;
- the only two services that generate additional income for the post offices are the driver's licence renewal and passport "checks and send".

Subvention

Subvention was introduced in the UK to account for the loss of income associated with the reduction in social welfare payments. Traditional income for the UK network decreased from £200 million to £80 million between 2003 and 2005 according to the NFSP. In 2013 the subsidy received by the network was £210 million (an increase of £30 million from 2012). While the post office has made a profit after tax of £49 million in 2013, without the subsidy the results of the 2013 financial year would show a loss after tax of £161 million.

The subsidy allows the government to fulfil its commitment to maintain the number of post offices at 11,500.[14] Ultimately, subvention shows transformation did not result in a sustainable network.

The post office faces a further round of closures, despite the significant cost to the UK government. Whilst subsidies may have helped in the short run, a long term solution is required.

Impact on Devon Communities

'Devon knows long term impacts and lessons from the post office Closure Programme' is a report into the impacts on communities in Devon of post office closures. The report highlights the detrimental impact on specific groups including the elderly and more vulnerable members of the community. The limited access to services as a result of the closures is a primary consideration of the report.

Also highlighted in this report is the economic impact experienced by the wider communities as a result of post office closures. The impact felt by the small and medium sized Enterprises (SMEs) is significant when local post offices close. SMEs provide employment in communities and rely on the network to post parcels, withdraw cash, and deposit takings. The post office closures mean that SMEs must now spend time travelling to other post offices. The costs (including time and fuel) for many small businesses appear to be significant; an extra burden at precisely the time when many SMEs may be struggling.

While the report analysed the impact post office closures had for Devon, it's fair to assume a similar impact could be expected in Irish communities should the network here begin to decline.

Conclusions

The UK post office faces an uncertain future. Whilst likely that the larger offices may survive, the stand alone rural post offices are unlikely to do so. A compulsory closure programme and the networks continued decline seem inevitable.

The loss of the welfare business in the UK saw revenue decline by 40%. The report on the impact of post office closures in Devon highlights the economic and societal repercussions these communities experienced, including increased difficulties for SMEs.

The UK government have so far not delivered on their commitment to increase government services provided by the Network and this is a factor that is contributing to the UK networks on-going decline. The UK government have used subvention to help the network there account for the loss of income associated with the reduction in social welfare payments. These subsidies at best provide a safety buffer for the post office while it is trying to establish more reliable long-term revenue streams.

There are a number of lessons we can take from the UK experience, these are explained overleaf.

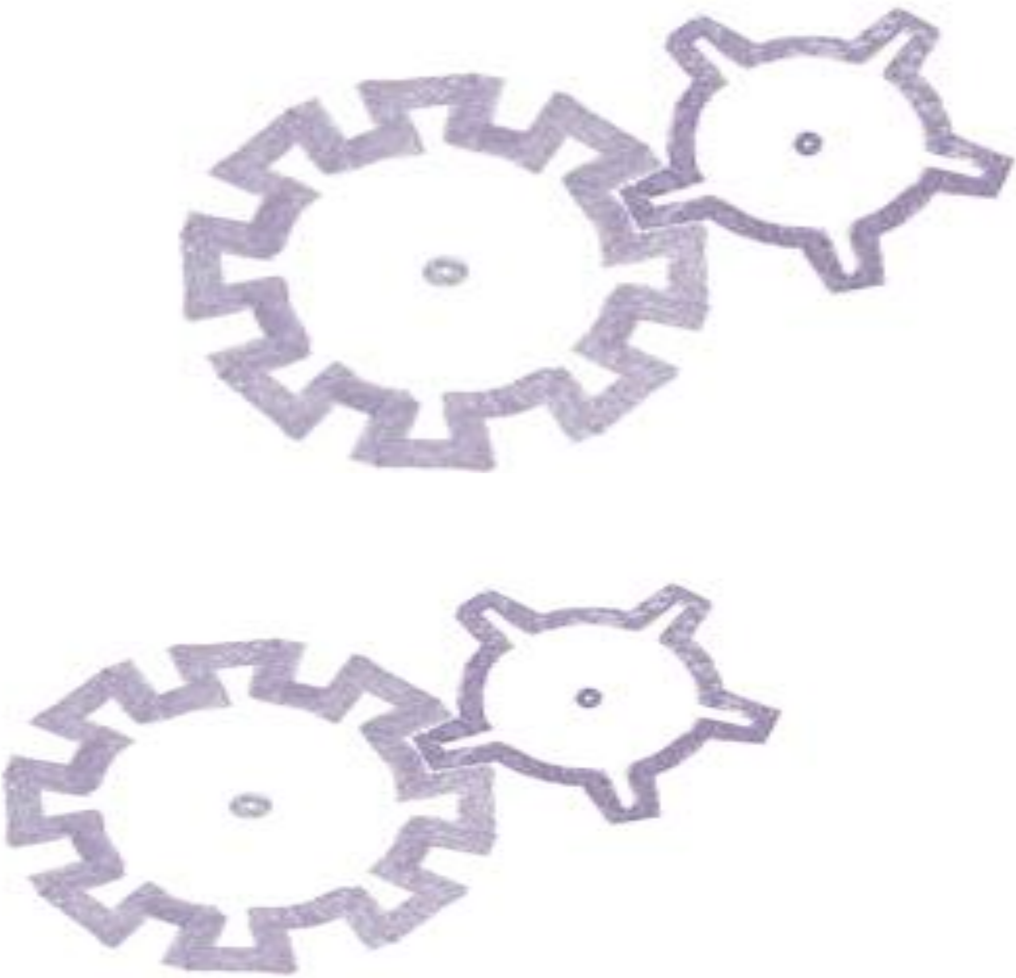
[14] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/31809/10-1260-securing-the-post-office-network.pdf

The main lessons that the Irish government can take from the UK experience are as follows:

Government must act to bridge the potential deficit facing the network or it cannot survive;

If continuing with its direct electronic payments policy, government should:

1. *design a model of direct electronic payments that meets the needs of both the DSP and the network;*
2. *allow for the creation of an exceptions list, so the public can opt out of electronic fund transfers continue receiving welfare payments OTC;*
3. *conduct an impact assessment, to understand the loss the network would have for Irish communities; and*
4. *consider subvention.*



5 Financial inclusion and the potential loss of the welfare contract

The government strategy for financial inclusion emphasises the importance of the move of social welfare payments to electronic format. This remains the most pressing issue for the network as the potential loss of the social welfare contract threatens its sustainability. This same strategy outlines the key role the network has to play in increasing financial inclusion in Ireland.

Without the revenue the welfare payments contract generates for the network, it cannot survive to play its part in increasing financial inclusion.

In this section, we review the impact of the move towards direct electronic payments of social welfare on the network and the wider Irish communities it serves.

Financial exclusion in Ireland

Below are key statistics regarding financial exclusion in Ireland.

Financial exclusion in Ireland key statistics:

- 9% of Irish population do not have a current bank account (Combat Poverty Agency Report)
- only 60% of the Irish population own a credit card. Both access to a bank current account and possession of a credit card(s) vary strongly with household income position;[15]
- 26% of low income households in Ireland do not own a current bank account;
- up to 84% of the income of low income households is made up of welfare payments;[16]
- 45% of social welfare payments are paid in cash through the network;
- 47% of the State pensions are paid in cash through the network; and
- 48% of Irish population live in rural areas.[17]

Financial exclusion remains a real issue in Ireland; almost 10% of population do not own a bank account. The overall take up of bank accounts is relatively high, but, 26% of low income households dependent on State support do not own a bank account and chose to use OTC services and cash payments.

Government has attempted to address the issue of low bank account usage rates in its Strategy for Financial Inclusion by proposing the introduction of the BPA.

The government hope that the BPA can provide access to affordable banking for low income individuals and facilitate the transfer of DSP and other State payments via EFT format.

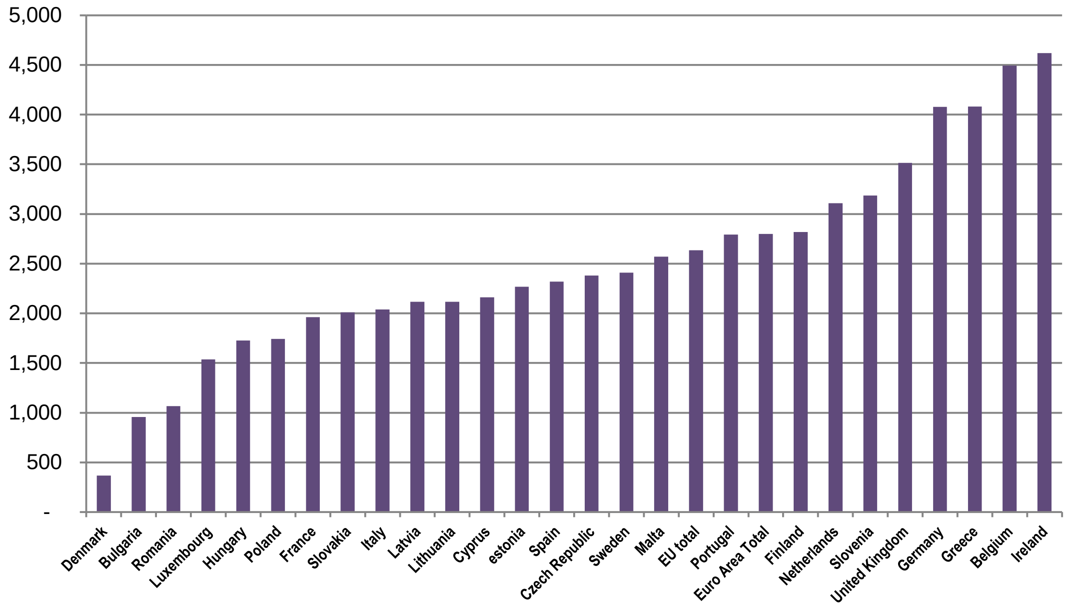
[15] http://www.socialinclusion.ie/publications/documents/2011_03_07_FinancialExclusionPublication.pdf
[16] http://www.cso.ie/en/media/csoie/releasespublications/documents/housing/2010/text.pdf
[17] http://www.cso.ie/en/media/csoie/census/documents/census2011vol1andprofile1/Census,2011, Population,Classified,by,Area.pdf

The Irish relationship with cash

As national and international statistics show, not all consumers are willing or able to adopt alternatives to cash. This can be for a number of reasons including demographics, habits and the ability to access financial services. It is likely that this would hinder the migration to electronic payment.

In Ireland, where cash is king, the country continues to have the highest usage rates of ATM's per capita (see figure 5.1 below) and the second lowest value of electronic credits in Europe.

Figure 5.1– ATM use in Europe



There are a number of reasons why consumers choose cash over electronic means of payment:

- some consumers have a low level of trust in the cashless system. People feel more comfortable dealing with cash rather than electronic transactions as it allows them to instantly assess the financial position of an individual;
- cash continues to dominate in minor OTC transactions;
- many small size retailers do not accept credit/debit cards payment for small transactions due to transactional costs or do not have the equipment to facilitate this type of payment;
- recent system failures and increased levels of card fraud have contributed to a low level of trust in the banking system;
- there has been a sharp decline in trust in the banking system and this resulted in large cash withdrawals by consumers who were afraid for the safety of their money;
- cash is accessible for all and still the only means of payment for the poor, under 16s and those not part of the banking system;[18] and
- people with smaller amounts of money typically find it easier to manage in cash.

It is inevitable that there will continue to be a need for OTC transactions in Ireland. The post office network is the largest network in the country and it can provide such a service. The provision of

[18] http://www.europeanpaymentscouncil.eu/article.cfm?articles_uuid=C9EAD88D-93E7-4671-5CCC09428816FC87

these same services by the network would be an important function considering the recent trend of bank branch closures particularly in rural areas.

The government must ensure it does not indirectly force further financial exclusion on already vulnerable members of society.

DSP contract overview

The delivery of social welfare payments directly to customer's bank accounts is a core component of the government's response to deal with financial exclusion.

At present the DSP contract to provide OTC social welfare payments generates over 30% of the network revenues annually. With declining income from the traditional mail, this revenue stream has become a critical dependence for the network. The loss of this contract would have a serious impact on the network.

Demand exists for OTC services. Currently 45% of the social welfare recipients choose to receive their support in cash at local post offices.[19] This is despite free availability of the EFT option.

The loss of the DSP contract and the introduction of e-Payments could potentially have a devastating impact on the network, and is likely to leave communities without access to many vital services.

Contribution of the network to their communities:

- *employment, the network has over 3,000 employees nationally;*
- *source of information, advise and governance;*
- *in many cases the only point of access to various financial services;*
- *point of support in accessing various services to elderly, unbanked and people unfamiliar with technology;*
- *supports local businesses and encourages employment by providing them access to financial, postal, and other services;*
- *retail shop is often a part of the business; and*
- *supports local businesses as consumers do not travel elsewhere to spend their money.*

To avoid financial exclusion, the networks long term sustainability needs to be addressed. This would ensure the network can continue to play a vital role in the financial inclusion of the communities it serves.

To better understand the implications the introduction of e-Payments would have three scenarios have been examined below:

- scenario 1 – No change – social welfare contract renewed and e-Payment strategy doesn't go ahead;
- scenario 2 – Social welfare contract lost – complete loss of revenues; and
- scenario 3 – Social welfare contract renewed but at a lower level of transactions due to the move to e-payment.

[19] Statistical Information on Social Welfare services 2012

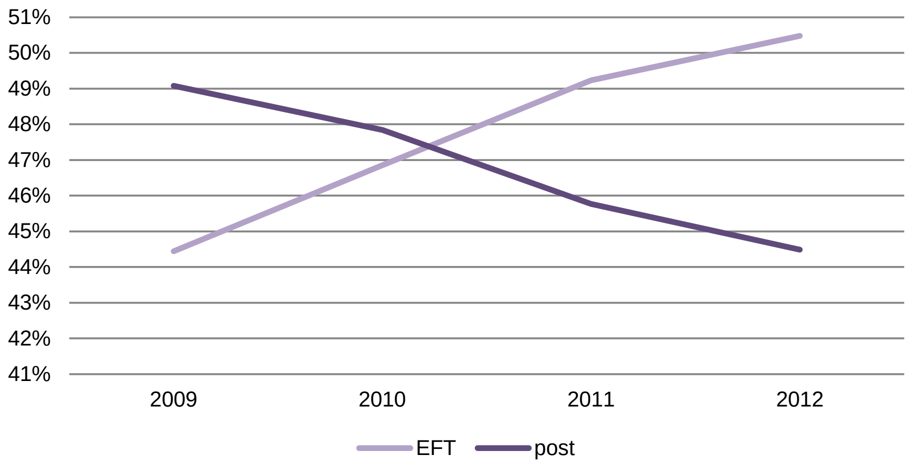
Scenario 1 – No change

In keeping with standard scenario planning, a counterfactual or "do nothing" scenario has been developed against which other scenarios are established, compared and appraised. We have based this scenario on calculations from the previous year.

This scenario assumes that An Post will retain the social welfare contract and e-payment initiative of the DSP does not go ahead and that the network would have sufficient time to gradually introduce new revenue streams to decrease dependence on OTC social welfare payments service.

The figure below demonstrates that there has been a gradual decline in the amount of social welfare recipients who chose to receive their payments at the post office while the number of people receiving their payments by EFT has increased.

Figure 5.2– Percentage of customers using post offices and EFT to receive social welfare payments, 2009-2012[20]



Source: Statistical information on social welfare services 2009-2012

The trends show that even under this most favourable scenario the network is likely to continue to see erosion in revenue it earns from the DSP contract. Despite this, the decline would be at a pace that would give the network additional time to consider alternative options, such as the provision of government front office and financial services.

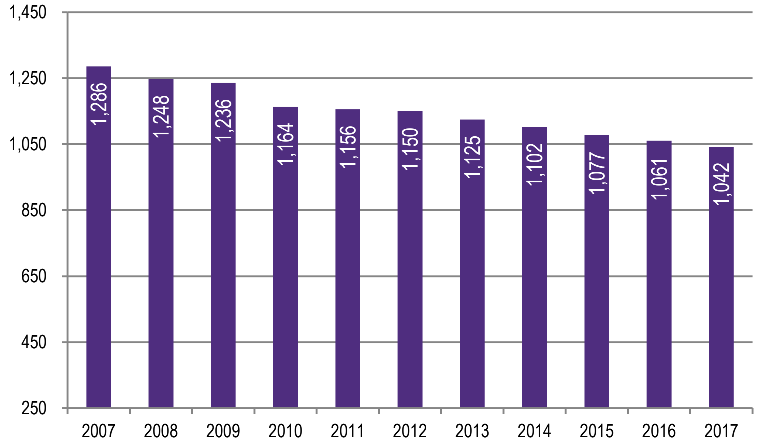
Table 5.1 – Scenario 1 – Summary findings

Scenario 1 - No Change	2012	2017	Office Closures	% Change
Network size	1,150	1,042	8	-9%
Social welfare transactions	43.60m	39.76m	-	-9%
Revenue generated by SW	€61.14m	€55.75m	-	-9%

Source: Grant Thornton analysis

[20] Statistical Information on Social Welfare Services 2009-2012

Figure 5.3– Scenario 1 – Projected post offices (2013 – 2017)



Source: Grant Thornton analysis

Scenario 2 – Social welfare contract lost

The second scenario is the worst case scenario. Under this scenario we have assumed that the provision of OTC social welfare services would not continue.

Whilst recent developments show that this scenario is unlikely to arise immediately, it highlights the implication of non-renewal of the contract.

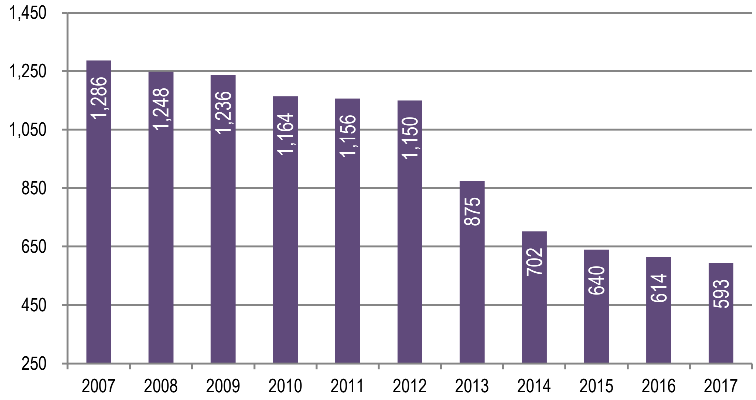
The loss of DSP contract will lead to network revenues decreasing by 30% which inevitably will lead to the closure of the majority of small to medium sized post offices (that may have up to 40% of their revenue generated by the DSP contract).

Table 5.2 – Scenario 2 – Summary findings

Scenario 2 - No change	2012	2017	Office Closures	% Change
Network size	1,150	593	557	-48%
Social welfare transactions	43.60m	-	-	-100%
Revenue generated by SW	€61.14m	-	-	-100%

Source: Grant Thornton analysis

Figure 5.4 – Scenario 2 – Estimated post office numbers



Source: Grant Thornton analysis

Any closure of small post offices would have a devastating impact on the communities where the post office remains the only point of contact with the government and performs functions of the local meeting, advisory and governance point. Such closures are also likely to have a wider economic impact in these communities as the repercussion of a lack of access to services becomes more pronounced.

In addition to this, closure of local post offices would increase the costs associated with provision of the universal postal services, as transportation and administration costs would increase significantly. Any closure of rural post offices would also contribute to the issue of rural unemployment.

Scenario 3 – DSP contract renewed and e-payment strategy introduced

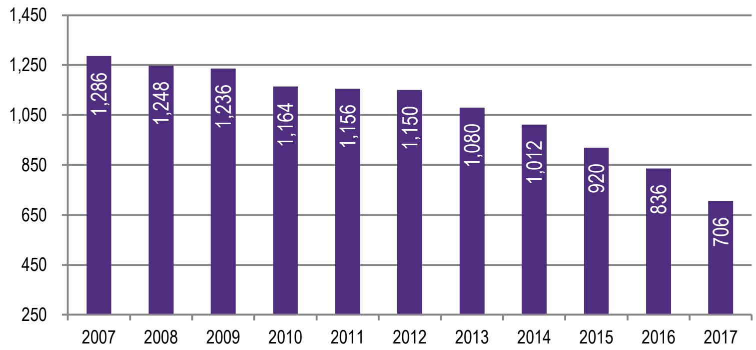
The third scenario is the most likely scenario. We assume that the network would be able to retain this important revenue source for the period of at least 2 years. During this time, an e-payment platform would be introduced by the DSP and cash payments may be gradually replaced by EFT. The process has to be supported by the provision of a BPA for the recipients of social welfare who do not own a bank account.

Table 5.3 – Scenario 3 – Summary findings

Scenario 3 - 75% e-Payments by 2017	2012	2017	Office Closures	% Change
Network size	1,150	706	444	-39%
Social welfare transactions	43.60m	9.94m	-	-77%
Revenue generated by SW	€61.14m	€13.94m	-	-77%

Source: Grant Thornton analysis

Figure 5.5 – Scenario 3 – Projected post office numbers (2013 – 2017)



Source: Grant Thornton analysis

Key implications for the network include:

- gradual decline of the revenue generated by DSP;
- decrease in footfall due to decline in customer numbers;
- closure of rural post offices if alternative revenue source is not created; and
- the network can bid for the e-Payments contract:

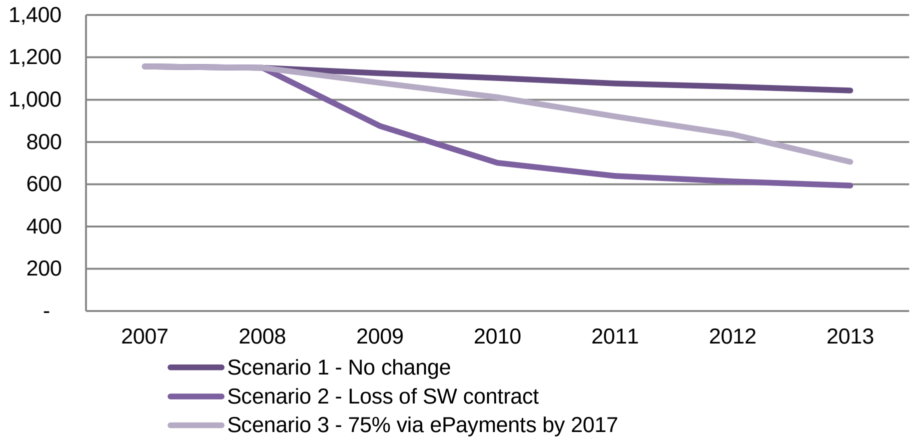
> *"I understand that An Post will pitch strongly for the social welfare e-Payments business when it is put out to tender. Having completed the computerisation of all post offices, An Post is well positioned to become the front office provider of choice for government and financial services sector."*
>
> *– Pat Rabbitte, Minister, Department of Communications, Energy and Natural Resources.*

Table 5.4 – Post office numbers scenario results

Network size	2012	2017	% Change
Scenario 1	1,150	1,042	-9%
Scenario 2	1,150	593	-48%
Scenario 3	1,150	706	-39%

Source: Grant Thornton analysis

Figure 5.6 – Projected post office numbers various scenarios



Considerations for implementation of current plans

The move to a cashless society and the introduction of specific initiatives such as e-Payments by the DSP would lead to significant challenges for consumers, the network, the government, retailers and other stakeholders.

To successfully implement the initiatives and ensure consumer buy-in, any change would have to be gradual, and account for other factors as follows:

1 bill payment: low income households and those dependent on social welfare typically manage their weekly bills through the post office, credit union, or the bank. According to our interviews with postmasters, the usual pattern is to pay the bills in person and in this case, the move away from cash is likely to adversely affect many families' ability to manage their budgets.

2 the failure of the BPA pilot, the culture of cash, continued bank branch closures and a lack of technical know-how when it comes to online banking mean that OTC welfare transactions would need to continue in same format if financial exclusion is to be avoided.

3 the move to electronic fund payments is likely to have a significant impact on the number of post offices across the county. Initial estimates would indicate that as many as 860 branches could close over a five year period. An impact assessment to identify and measure such repercussion for communities needs to take place.

4 introduction of the BPA and payment of social welfare by EFT may result in a sharp increase in welfare payments fraud. ID would be required to open a new BPA, yet EFT does not require a compulsory ID verification.

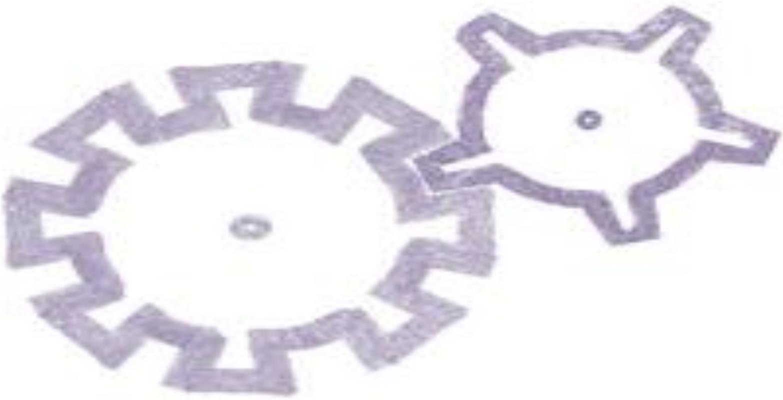
Conclusion

The DSP contract to provide OTC social welfare payments generates over 30% of the networks annual revenue. In any of the chosen scenarios the decline in revenue for the network has stark implications for its future sustainability.

Conscious of the governments' attempts to increase financial inclusion and to move towards a less cash dependent society there needs to be appropriate products available to those customers that do not have access, or wish to use bank accounts.

A BPA offered by the network in conjunction with the administration of an 'exceptions' list via OTC could assist the government in realising their objectives. The opportunity to provide BPA through the network is discussed in detail in section 7.

All of the scenarios outlined indicate the stark reality facing the network into the future. Post office closures would be inevitable and the most affected will be the 860 small to medium post offices, mostly located in rural Ireland. The impact to rural communities will be vast and further economic impacts for these areas as a result of post office closures can be expected.



6 Banking

The network is seeking to expand its financial service products offering. However, revenues gained as a result of this will not be sufficient to replace revenue lost due to changes in the welfare contract.

In this section we explore the role of the network in the provision of financial services. Also outlined are possibilities for the extension of financial services offered by the network. This analysis includes the BPA, and looks in more detail at a proposed model for its introduction.

The role of the postal network in providing financial services

The network has provided basic financial services to communities for many years. There is widespread consensus that additional financial services could be added to the current service offering.

Banks, responding to business challenges resulting from the economic crisis, are continuing to downsize. The growing trend of bank branch closures means the role the network can play in the provision of financial services grows at pace.

At present the network offers a number of banking services to their customers through their partnerships with Allied Irish Bank and National Irish Bank.

Table 6.1 – The role of the Irish postal network in providing access to financial services

Payments	Receipt of social welfare
	Access to banking services through AIB and Danske (formerly NIB)
	Bill payment through Billpay
International remittances	Postal money orders
	Foreign exchange
	Western Union transfers
	Eurogiro
	Sterling draft
Savings	State savings available through NTMA
	National Solidarity Bond
	Prize Bonds
Insurance and pensions	Insurance with One Direct at An Post
Lending Services	None

Extension of banking services

There are a number of areas where the network can extend its financial service offering. These include:

- the BPA;
- additional partnerships; and
- the formation of a strategic alliance with the credit union.

The basic payment account

It is envisaged that direct electronic payments of social welfare would occur in line with the introduction and roll out of the BPA. This will facilitate transfer of the social welfare cash payments via EFT directly into customers' bank accounts.

Grant Thornton believes that the government should consider the costs involved in the roll out of the BPA and whether or not this would be any more cost efficient than the current OTC service? Also the question arises as to who would bear the cost of operating the BPA?

If the primary reason the government is proceeding with the BPA is financial inclusion, then the government needs to also consider the commercial viability of the network, which as a result of the loss of the welfare payment contract would have declined. In such circumstances the ability of government to improve financial inclusion would be hampered as a consequence of this reduced network and financial exclusion will rise.

Coupled with the trend of bank branch closures, this means even more people would find themselves financially excluded. The prospect of increased financial exclusion becomes even more real when those without the access or the technical knowledge to conduct transactions digitally are accounted for.

If government decide to proceed with direct electronic payments then the network needs to be part of the solution.

A desired model for the introduction of the BPA and the move to EFT social welfare payments is explored below:

- identify who would bear the cost of the BPA;
- clarify if this would be any more cost effective than the current OTC service delivery mode; and
- if proceeding with the introduction of a BPA:
  - BPA should be made available through the network, to facilitate those receiving payments;
  - the default option being a direct electronic payments via EFT into a BPA; and
  - include an opt out clause that allows for the continuation of OTC services for welfare payment.

Unless established as a bank itself, An Post would not be able to offer customers transactional banking services without the support of a specialised financial institution. It is of paramount importance that the BPA is provided by all the banks and possibly credit unions and that consumers are able to apply for it in a post office of their choice.

If introducing direct electronic payments government need to include the provision of an opt out clause. This opt out clause can be used by those customers who do not wish to receive their payments through a BPA.

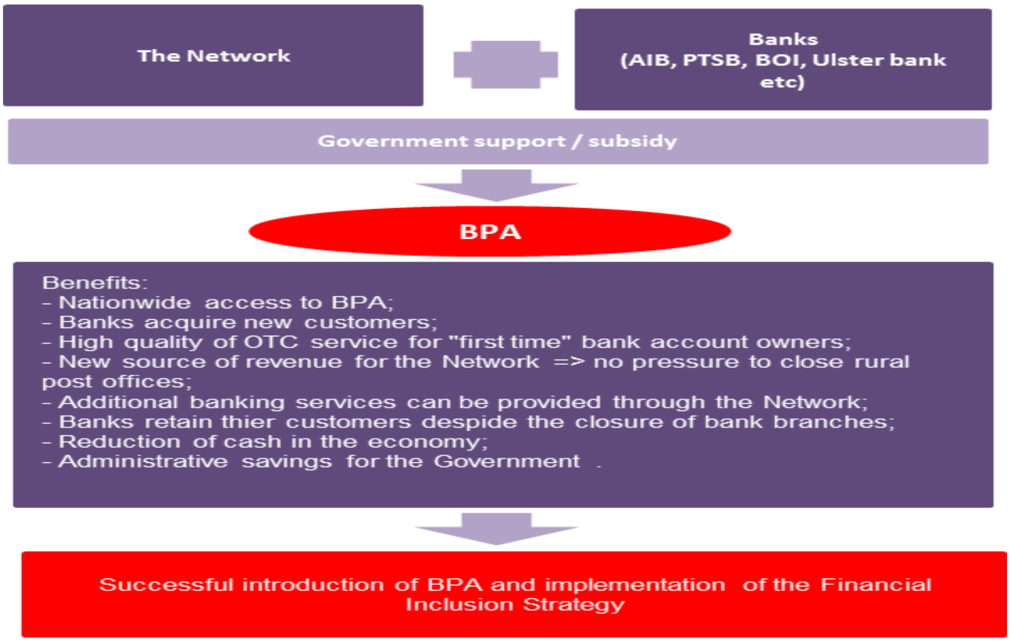
The provision of an opt out clause would retain some revenue for the network. The DSP and the network should make sure that a form is available at the local post offices for those customers who want to revert to payments through the network. As has been the UK experience the revenues generated in this way would not be sufficient to compensate for the overall decline in revenue.

Allowing for an opt out clause enables government bring financial inclusion to those without the access or technical knowledge to execute financial transactions online. The extent of the financial inclusion that can be realised in this way is dependent on the network retaining its size and geographic spread.

As the account would have no fees or charges, there is no financial incentive for the network to be included in the process. The provision of a BPA service would have to be met by the government or via a levy on the banks to ensure that providers will be compensated for any extra costs[21].

Further thought would be required to understand the impact the introduction of a BPA would have on household finances. Currently, bills are paid in person on a weekly basis at the post office; replacing this with a direct debit system brings with it concerns that a poverty trap will be created.

Figure 6.1– Desired model



[21] http://www.tcd.ie/policy-institute/assets/pdf/BP26_Financial_Exclusion_Gloukoviezoff.pdf

Provision of BPA through the network would generate significant benefits for the government:

- access to BPA for those living in rural parts of the State;
- increased financial inclusion, particularly in light of recent bank branch closures;
- public has a higher trust in the network than in the banking institutions;
- existing DSP customers would not have to change their habits of receiving payments at the local post office; and
- no one bank would be able to offer the level of customer service and support the network can offer in the transition process.

Additional partnerships

The network offers a wide range of financial services. In the previous report we have identified that there is capacity to expand this service line by partnering with more banks.

Our analysis last year showed that if Bank of Ireland (BOI) and Ulster bank partnered with the network the total benefit generated over five years will be as high as €7.7 million, with almost €4.5 million benefit attributed to the banks.

AIB and Danske Bank are already providing their services through the network and some other major banks have expressed their interest in exploring this opportunity.

Permanents TSB in its submission to the Joint Committee on Transport and Communication stated that from profitability and shareholders perspective the bank is not able to extend its network to the rural areas and partnership with An Post for distribution of banking services may be a possible solution.[22]

Services offered via the NTMA contract could also be extended to include a universal pension account.

Strategic alliance with the Credit Unions

A partnership with Credit Unions would allow the network to offer credit services. Credit Unions are currently undergoing significant challenges that threaten their long term sustainability. Both the Credit Union and the network have to expand their service offerings to secure their sustainability into the future.

Credit Unions would benefit from the partnership with the network offering a large distribution channel for their products thus increasing their customer base while the network would have a new revenue stream and will increase footfall.

From a strategic perspective, there are significant synergies for both the network and Credit Unions. Both, Credit Unions and the network, carry important social functions, both have retained the trust of the public and that makes them a core element of Irish communities.

While this solution provides a great opportunity for the network and Credit Unions, there are significant barriers to its implementation. The major issue would be the high level of independence amongst the Credit Unions and the lack of uniformed systems and processes to support provision of shared services. However a partnership with selected credit unions and An Post could provide a viable short to medium term opportunity.

[22] Joint Committee on Transport and Communications Report on promoting a Sustainable Future for the network. March 2013

A further study of this opportunity needs to be carried out in order to identify whether it is feasible to establish the alliance.

Conclusion

The network can expand its current financial service offering. However, the financial deficit the network is facing cannot be bridged through the provision of additional financial services.

Government must clarify if the provision of the BPA can realise saving for the exchequer when compared to the current OTC format. If the primary driver towards the roll out of the BPA is financial inclusion, then the impact the loss of the social welfare contract will have on the network and the subsequent repercussion for financial inclusion need to be examined in greater detail.

The network has a role to play in the roll out of the BPA. The ideal model for the implementation of the BPA has been outlined.

Other areas of potential growth include partnerships with Bank of Ireland, Ulster Bank and Permanent TSB. These potential opportunities need to be advanced. An alliance with the Credit Unions would be appealing but could take some time to mature.

7 Government front office

It's important the network continues to retain and expand its services as a government front office. Analysis suggests this would not generate sufficient revenues to compensate for the loss of the social welfare contract.

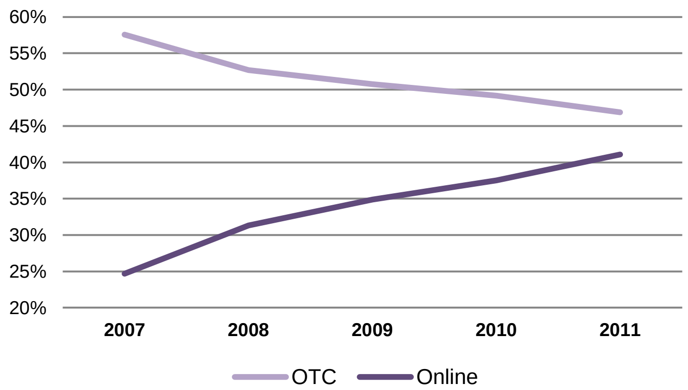
At present a variety of government services are successfully provided through the network. These include: Passport express, TV licences, social welfare payments, NTMA savings, the property tax, dog licence and Garda fixed fines. All can be processed through the local post office. Yet the network has the capacity, facilities and capabilities to accommodate the provision of further government services and in doing so, can support the delivery of those services especially to rural areas.

The government remains under pressure to realise expenditure savings and to ensure a more sustainable public service into the future. Whilst these challenges are significant, they do offer opportunities for both the government to create efficiencies and for the network to build upon its position as a trusted government front office.

Motor taxation

The provision of motor taxation is the most realistic and achievable option for increasing government front office services that could be provided by the network. Based on the current strengths of the network and the requirement for efficiencies in local government as a result of the Croke Park agreement, the network could easily facilitate payments to be made using cash, cheque, debit card or credit card and at the same time reduce the administrative costs associated with the processing of motor tax transactions. The level of people who require OTC service remains significantly high at 45% as outlined in the service indicators for local authorities 2007 – 2012

Figure 7.1 – Motor Tax transactions by type



Source: Service Indicators in Local Authorities 2007-2011

In a value for money review carried out by the Department of Environment and Local Government, the cost of delivery of motor tax was estimated to be in the region of 5.8% of total income received. Whilst it is likely that this number has dropped due to the continued move online and the closure of a number of motor tax offices, there has not been any other significant changes to the administration structure of the network. This would therefore suggest that it could be costing the local authorities somewhere between €15 and €20 per OTC transaction.

Based on other similar services, it would be reasonable to conclude that the network could provide this service at a fraction of the same cost (circa €2 per transaction). A simple analysis shows the potential for significant savings for the local authorities. Based on current OTC transactions, this would result in a potential saving of €26 million per annum (based on the OTC revenue for 2012) for local authorities. Note savings include both domestic and commercial renewals.

In a more detailed analysis prepared in our previous report, Grant Thornton estimated that there was an even greater additional benefit for the government over five years if motor tax collection is introduced through the network. The cost-benefit analysis estimated that there was potential to generate an additional benefit of over €63 million over 5 years; with over €46 million attributed to the government and a further €17 million for An Post. The potential annual savings could reach €27 million (PV year 5 in table below), which is broadly in line with the basic calculation above

Table 7.1 Potential benefits – motor tax

		TOTAL	2013 Year 1	2014 Year 2	2015 Year 3	2016 Year 4	2017 Year 5
COMBINED (network and government)			**€'000**	**€'000**	**€'000**	**€'000**	**€'000**
Benefits	Operating income	**19,720**	1,360	2,720	4,080	5,440	6,120
	Staff savings	**73,444**	4,896	12,241	14,689	19,585	22,033
	Total Benefits - Motor Taxation	**93,164**	**6,256**	**14,961**	**18,769**	**25,025**	**28,153**
Costs	IPU/An Post service charge	**19,720**	1,360	2,720	4,080	5,440	6,120
	IT costs	**122**	122	-	-	-	-
	Staff costs	**661**	660	0	0	0	0
	Bank charges	**1,183**	82	163	245	326	367
	Postage costs	**5,610**	374	935	1,122	1,496	1,683
	Total costs - Motor Taxation	**27,296**	**2,597**	**3,819**	**5,447**	**7,262**	**8,170**
	PV Benefits	**89,581**	6,016	14,385	18,047	24,063	27,070
	PV Costs	**26,246**	2,497	3,672	5,237	6,983	7,856
	NPV, Benefit/Cost ratio	**63,335**	**3.41**				

Since our previous report there have been no material developments that would cause us to revise our estimate. The one potential impact could be the legislation change for the off-road vehicles, however as there is no data available to show how this would affect the OTC numbers we have not included it.

Other options

Although motor tax offers the greatest potential for the network, there are a number of other potential options that could be provided and should be considered by both the government and the network.

In this section we look the other opportunities that should be considered by the network and the government.

These are:

- electronic government forms; and
- driver's licence.

Electronic government forms

Government agencies continue to move towards online service delivery channels. Traditionally paper-based forms are now available online and consumers are encouraged to complete and submit them online. For instance, revenue requires mandatory online filing/payment for 16 types of tax returns.[23]

A Consumer Futures survey carried out in UK identified that government forms (ability to access, complete and submit them) is the most preferred service that the network could provide. Similar consumer preferences can be expected in Ireland.

New services the network could offer include:

- submitting government or council forms;
- access to government and council forms for those without internet access;
- "check and send" service;
- help in filling out official applications; and
- help with online applications.

Whilst the demand for the new service is expected to be high, further research would be required to assess whether benefits will exceed the costs associated with setting up and running of the service.

It is not possible in this report to provide an accurate cost benefit analysis of this opportunity due to a high level of unknown variables.

A pilot could be carried out in selected post offices across the country to identify the revenues that can be generated and cost associated with the service. A selection of statutory forms of different complexity could be offered to the customers.

The table below summarises the key pros and cons of introducing the service at the local post offices:

Table 7.2 Pros and Cons – government forms

Pros:	Cons:
• increase efficiencies in government departments by reducing the amount of incomplete/unreadable applications; • drive more customers to the network; and • assistance to consumers who do not have access to internet or are not familiar with the technology.	• expensive and time consuming training for the network staff; • there is a significant amount of statutory forms; • in order to ensure consistency in the service offering access to all the forms has to be provided; and • completion of the forms may be very time consuming, while the margin will remain small.

[23] http://www.revenue.ie/en/online/ros/mandatory-e-filing.html#section2

Driver's licence

One of the government services provided through the post offices in the UK that generates income for the network is support of the driving licence application/renewal process. In the UK, provision of this service generates up to 20% of individual post offices' revenue.

Recent developments here mean those applying for, or renewing licences can no longer do so by post without having already attended one of the newly created national driver licence centres. A reduced number of 34 centres for renewing licences and issuing learner permits exist and transactions need to be completed face to face with the applicant. This development has been met with criticism in the media as it leads to increased waiting times, and longer distances from services for many.

The network could be another point of access to the service in the same way as the post office in the UK. It could receive the documentation, check it for errors and pass it on to the motor tax office.

Due to the lack of an online facility to apply for a driver's licence in Ireland (in the UK an application can be submitted by post, online or at the post office). It is possible that even greater demand might exist for access to such services if offered by the network.

Introduction of this service at the local post offices could partially replace the declining revenues from the DSP contract. In addition no significant capital investments or training costs would be required to roll out the service. The network already plays a key role in the renewal of passports and a similar service in the renewal of driver's licences would be both consistent and complimentary to current service offerings.

Conclusions

The expansion of government front office services provided by the network should continue. Government need to push more front office services through the network. However the revenue generated by these additional services will not compensate for the loss of the welfare contract.

Motor taxation is by far the most suitable of government front office services the network can provide. Given the cost associated with the provision of this service for the local authorities and bearing in mind the reductions being sought under the Croke Park and Haddington Road agreements the network could be best placed to deliver this service for the substantial number of individuals who continue to utilise the OTC facility.

There is consumer demand for the network to provide access to, assistance with and submission of government forms. Cost benefit analysis would be required before this option is progressed further. In a similar vein the network could provide services in respect of driving licences based on the existing passport express model.

8 Conclusions

Despite continued assertions by government officials as to the importance of the post office network, little support is being offered to it.

Should the network lose the contract to deliver welfare payments it would suffer a financial deficit which cannot be bridged solely by increasing financial or government front office services.

The network would face inevitable closures if these developments proceed as planned.

Table 8.1 – Scenario findings

Network size	2012	2017	% Change
Scenario 1 – No change	1,150	1,042	-9%
Scenario 2 – Loss of SW contract	1,150	593	-48%
Scenario 3 – 75% e-Payments by 2017	1,150	706	-39%

Any such impact on the network will have significant repercussions for financial inclusion. A weakened network would contribute to financial exclusion.

In reconsidering direct electronic payments, the government should address how direct electronic payments would perform the fraud function the current OTC service delivers and address such a function as effectively and realise savings as directly.

For the network to continue the role it plays in Irish life, the government must re-examine its pursuit of direct electronic payments, and be conscious that the network will not survive without the €60million per annum this contract delivers for An Post and in particular the €20 million relied on by the Postmasters.

Before introducing a BPA it needs to be established if this method of service delivery is any way more cost efficient than OTC payments. The party that would bear the cost of the BPA also needs to be identified. A model for the introduction of the BPA and the move to EFT social welfare payments is explored below:

- identify who would bear the cost of the BPA, and
- clarify if this would be any more cost effective than the current OTC service delivery mode;
- if proceeding with the introduction of a BPA:
  - BPA should be made available through the network, and be the sole source of social welfare payments;
  - the default option being a direct electronic payments via EFT into a BPA; and

- include an opt out clause that allows for the continuation of OTC services for welfare payment.

Methods for retaining the network could include the continuation of the welfare contract, and subvention to replace the €60million per annum lost as a result of the network losing the welfare contract.

Outlined below are reasons the government should seek to retain the network as – is:

- the fraud deterrent function completed by the network, including refunds to the DSP in relation to uncollected welfare payments cannot be replicated in a direct electronic payments model;
- the inadvertent contribution the decline of the network would have in increasing financial exclusion;
- the network employs over 3,000 people; and
- the intrinsic and unquantifiable role played by the network in Irish communities and its impact on their economic well-being.

The key findings of the report are as follows:

Table 8.2 – Key findings

Key Findings

• the networks future sustainability is at risk owing to changes in government contracts due for renewal. The contracts in question are:
  • the social welfare contract; and
  • NTMA savings.

• the social welfare contract is worth €60million per annum to An Post with €20 million of this accruing directly to the network. The network cannot survive without maintaining its current revenue.
• options to expand the financial services and the evolution into a front office for government services are critical to the network. However these alone would not deliver sufficient revenue to sustain the network when accounting for the loss of the welfare contract.
• learn from the UK experience where a move to direct electronic payments of welfare and failure by government to deliver additional services and business for the network has contributed to its decline.

• Before embarking on a system of direct electronic payments Grant Thornton would call on the government to consider:
  • the cost savings direct electronic payments has over the current OTC method;
  • the inadvertent contribution direct electronic payments would have to financial exclusion;
  • fraud risk, and loss of control associated with EFT payments; and
  • the impact on citizens and communities including the economic consequences for the community if the network is left to deteriorate

Before introducing a BPA it needs to be established if this method of service delivery is any way more cost efficient than OTC payments The party that would bear the cost of the BPA also needs to be identified. A model for the introduction of the BPA and the move to EFT social welfare payments is explored below:
• identify who would bear the cost of the BPA, and
• clarify if this could be any more cost effective than the current OTC service delivery mode;
• if proceeding with the introduction of a BPA:
  • BPA should be made available through the post office network, and be the sole source of social welfare payments;
  • the default option being a direct electronic payments via EFT into a BPA; and
  • include an opt out clause that allows for the continuation of OTC services for welfare payment.

• scenario 1, if there is no change to existing government contracts and network revenues remain stagnant then the number of post offices would decline from 1,150 at present to 1,042 by 2017; • scenario 2, if the network loses the social welfare contract only 593 post offices may remain in 2017, representing a decline in network size of 48%; and • scenario 3, if direct electronic payments is introduced and 75% of payments occur via EFT without the involvement of the network, with the remainder delivered via OTC by the network then only 706 post offices may remain by 2017, representing a decline in network size of 39%.
• to sustain the network government needs to act now and in so doing address the issue from the perspective of both economic and social policy.

Grant Thornton

An instinct for growth™