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Royal Mail 'John Lewis' Scheme to Cost Taxpayers Billions *(REVISED)*

Issues and errors associated with the Royal Mail 'John Lewis' proposals are presented and briefly discussed, as well as the wasteful multi-billion pound price tag UK taxpayers will ultimately incur (suffer) as a result.

The Lib-Con Government (Lib-Con) is considering essentially what the Labour Government before them tried, namely, bribe—sorry, payoff—sorry, it is proving difficult to obtain the correct word to accurately and properly define—inveigle, that is the word—inveigle certain participants in the battle to lessen a portion of the opposition to proposed plans to gain legal approval to sell, all or part of, Royal Mail—the so-called 'John Lewis' Ownership scheme (the "JLO").

In late April of 2009, then Business Secretary Lord Mandelson introduced the Labour government's poorly conceived attempt to circumvent union opposition to a partial sale of Royal Mail with their so-called 'John Lewis' Compromise (the "JLC"). The Postal Services Bill (the "PSB") proposed authorising the sale of up to 49% of Royal Mail, with 30% to be sold immediately. With continued fierce postal union opposition to the sale of Royal Mail, Lord Mandelson introduced the so-called JLC, giving the remaining 19% of Royal Mail (i.e., 49%-30%) to the union. Of course, the inveigle JLC was rejected by the postal worker's union. In fact, the inveigle JLC was not a compromise at all, as outlined in the 14 October 2009 Hellmail article entitled, "Beyond the Hooper Report" and a 30-page report dated 17 June 2009 entitled, "RMG [Royal Mail Group] Part-privatisation Analysis; Modernisation, universal service and pension reform."

Lib-Con's approach, the JLO, is reported to offer ownership to postal workers this time. In that respect, the JLO and JLC differ; however, the JLO, like its predecessor, the JLC, have serious issues that are not mentioned or disclosed, excluding my discussions on the subject of course. Since exact numbers (details) of Lib-Con's JLO have not been disclosed as yet, Lord Mandelson's JLC is sufficient to demonstrate the serious issues and costs associated with these inveigle 'John Lewis' proposals.

Presuming a 30% sale of Royal Mail was able to generate £3 billion in a 2009 sale, and the union accepted the 19% ownership offer from Labour's inveigle JLC (in exchange for dropping their opposition to the sale), the result would have been a three-way ownership (19% Postal Union/30% investor/51% UK Government). Furthermore, the union's 19% ownership would be valued at £1.9 billion, although no actual monies would be exchanged (note, it does not matter what amount the 30% generates, the union's ownership value would be proportional,

and therefore equal to 19%).

Only four select issues are presented, although others certainly exist. First, any future sale by the UK Government would relinquish majority control. Second, the resulting structure will likely complicate both operational decisions and any future sales, dwarfing the challenges the original sale presented. Third, UK taxpayers unnecessarily donated 19% of the country's postal service. Fourth, the change in shareholder equity in accounting terms equates to only £1.1bn, far short of the £4.9bn the relinquished 49% ownership was actually worth. That is, the UK Government (i.e., taxpayers) would give up cash generation on close to 20% ownership (valued at £1.9bn) in order to sell 30% (valued at £3bn). The inveigle JLO results in an extremely high valuation loss by anyone's definition. It is only £1.1bn because the £3.0bn total raised is offset by the £1.9bn given away, resulting in only £1.1bn! This is not an accounting trick, for the £1.9bn has to be deducted when it is given away.

Put another way, to reduce some but not all opposition to the planned sale of Royal Mail, the UK Government will forego about £2.0bn in cash (giving up nearly 20% ownership) in order to pursue a mere £3.0bn in cash (selling 30% ownership), thereby relinquishing 49% ownership (a near majority) and reducing the government's ownership valuation by nearly half (£10bn before, to only £5.1bn after) for an accounting gain of only £1.1bn instead of £4.9bn. Seriously, the scheme is an utterly ridiculous and absurd business transaction to pursue; yet, it keeps being proposed in one form or another!

In the case of Labour's failed inveigle JLC, the intent was to give the union part ownership in Royal Mail, incorrectly assuming the union would take ownership in exchange for dropping opposition to the sale. Lib-Con's intention is clear, by giving postal workers part ownership in Royal Mail, postal workers would be less likely to support, or agree to, any union calls for national postal industrial action over the issue of selling Royal Mail, thus supposedly limiting or mostly squelching the fiercest single organised opposition to any Royal Mail sale. Unfortunately, both JLO and JLC schemes are seriously erred.

The errors are the result of failing to fully understand the dynamics of the problem set, and using a defeasible argument and flawed logic to arrive at a proposed scheme that only circuitously links the premises and conclusion. First of all, the union is not the only opposition to a sale of Royal Mail. Second, the primary objective of the sale is to generate cash; therefore, unnecessarily giving away a significant portion of ownership defeats the primary objective (intended purpose). Third, the targets for the JLO (postal workers) and JLC (postal union) and the opposition the schemes are meant to deflect are only indirectly and partially linked. Although only three errors are briefly outlined here, others certainly exist, and each clearly demonstrates the problem set, proposed remedy and the logic in arriving at the proposal contains many serious errors.

Furthermore, because the JLO proposes giving ownership in Royal Mail to postal workers instead of the postal worker's union, as in the JLC, there is another issue specific to the JLO, and one I suspect most have not even remotely considered as yet. The JLO is meant for postal workers, or more appropriately, for currently employed postal workers. From March 2009 through March 2010, there were 8,051 fewer postal workers, all of which are excluded from the JLO, and then, there are all those that lost their postal jobs prior to March 2009. No matter what end-date is set for inclusion in any JLO, thousands of former postal workers will be excluded. For some of them, the exclusion will create quite a divide, with those feeling wronged likely to turn to one of two real voices for opposition. Regardless of the voice chosen, the opposition will likely be against the overall sale, and not against the JLO itself.

Any 'John Lewis' proposal should focus on fairness and appropriateness, and not on the issue of lessening opposition. To even entertain the ridiculous notion that the 'John Lewis' proposals are not opposition based is to deny reality. Ignoring facts or accepting rhetoric and

deceptive political games will not solve problems, and history provides the proof, over and over again. Actually, from 1935 through 1939, one man's facts and applicable warnings were repeatedly ignored and marginalised by officials from three different governments (including the man's own political party) concerning England's military strength versus Nazi Germany's rapid post-World War I (WW-I) military build up, clear violations of the treaty that ended WW-I, and Germany's pre-World War II ambitions to dominate Europe. The man's facts and warnings were ignored almost to the point of total loss for England and Europe, unless of course, you subscribe to the belief of denying reality. The man was Sir Winston Churchill.

Moving on, Royal Mail is a government entity, ultimately owned by all the people. Therefore, any significant distribution of a public asset to non-public entities is fundamentally flawed unless said distribution can adequately identify each person's financial contribution, thus dividing the designated percentage of total ownership proportionally to each person. Clearly, the task is impossible as defined; so only two logical possibilities exist for offering a Royal Mail 'John Lewis' shared ownership proposal. Furthermore, the issue of adequate compensation for postal workers is a fair and reasonable one, but transferring a significant portion of public ownership to a select portion of the population is the wrong way to resolve the issue. There are more appropriate means of accomplishing adequate postal worker compensation.

There are additional issues and errors with the JLO, but realistically, what is already presented is sufficient to warrant no action on continuing the idea of any 'John-Lewis' ownership proposal as presented by the government. Does a strategy exist whereby union opposition to the sale of Royal Mail could be mitigated such that national industrial action by the union is avoided? *Absolutely, make no mistake, there are appropriate strategies that will reduce or lessen most opposition, to include union opposition, to any sale of Royal Mail. That is not to say that opposition, including union opposition, will completely dissipate upon execution of an appropriate strategy.*

In simplified terms, if all aspects of a problem set are not fully and completely understood, then any resulting strategies will likely be equally deficient, with a successful outcome statistically improbable and merely coincidental. Case in point: Presume you have a teenager that enjoys playing videogames with a persistently messy room. You propose giving said teenager an hour and a half of extra time for television viewing if they keep their room clean. The result is only sporadic compliance. On the other hand, if half an hour were allotted for video games, the room would remain clean. The point is merely to show that understanding the full scope of a problem set is critical to solving problems.

The 'John Lewis' proposals are just one of the many erred issues relating to the overall modernisation effort for Royal Mail. Managing a distressed turnaround, especially when the distressed business also operates in a distressed market, is unlike managing any other business operation, and if not properly managed, failure will result. In conclusion, any significant ownership re-distribution of Royal Mail, whether free or partially subsidised, using an inveigle 'John Lewis' scheme is an utterly wasteful, unnecessary and costly expense ultimately financed in whole by UK taxpayers for a select few.

About the Author: Timothy Nestved is founder and president of Nestved LLC, as well as a principal consultant, with expertise in turning around firms in the delivery services industry, including distressed firms facing similar challenges to those of national postal service providers like the Royal Mail and USPS. Inquiries for Timothy may be submitted through the Contact Us page at Nestved, LLC.

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