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Our Ref : LS/CT 74000

27th April 2010

RECEIVED

29 APR 2010

Mr Paul Hamilton
Jersey Competition Regulatory Authority
Second Floor
1-9 Salisbury House
Union Street
St Helier
Jersey JE2 3RF

Dear Mr Hamilton,

RE: COMMUNICATION WORKERS UNION – SUBMISSION TO JCRA CITIPOST AND HUB EUROPE LICENCE APPLICATION

The Communication Workers Union has considered your recent announcement regarding the issuing of a licence to the above postal businesses.

We have attached for your information, a copy of our submission to you on this matter. This submission sets out our views and comments in some detail. It is important that you understand and recognise the CWU's outright opposition to your proposal. We believe, as an organisation, that your proposal will damage and seriously threaten the long-term viability of Jersey Post and in turn our members' future employment. We also believe that your proposal will lead to a weakening of the USO and the worsening of the island's postal service.

The CWU feels so strongly about this matter, that we intend to organise an aggressive campaign with the island's population, with the aim of reversing your proposal.

In closing, the union has, as we've already stated in previous submissions, been quite prepared to meet with your organisation and expand upon any of the points that we've detailed in our submission to you.

Yours sincerely,

Peter Donaghy
Vice Chair
Postal Executive

CWU RESEARCH

Submission to the JCRA – Citipost and Hub-Europe initial decisions

Introduction

1. The Communication Workers' Union (CWU) represents 250,000 employees in the postal, telecommunications and financial services industries. We are the recognised union for postal grades in Jersey Post and have 276 members in the business.

2. In May 2009 the CWU responded to the Jersey Competition Regulatory Authority's (JCRA) consultation on a Class 1 Licence Application from Citipost DSA Ltd ('Citipost') opposing the award of such a licence. We are disappointed at the Initial Notices published by the JCRA on 31st March 2010 to grant bulk mail licences to both Citipost and Hub-Europe Ltd ('Hub-Europe') and urge the JCRA to reconsider both of these decisions.

3. The CWU strongly believes that the introduction of competition should remain subordinate to maintaining a viable universal service which meets the needs of the public and businesses. The JCRA's decisions to grant bulk mail licences will jeopardise the future of the universal service in Jersey and we believe that it has failed in its duty to adequately assess the impact of this.

The JCRA's primary duty

4. In accordance with article 8 of the Postal Services (Jersey) Law 2004 the JCRA's primary duty is to ensure that postal services – including the universal service – which satisfy all current and prospective demand are provided within Jersey having regard to the quality, affordability and accessibility of such provision. The CWU does not believe that the JCRA's decisions to grant licences to Citipost and Hub-Europe are in line with this obligation.

The universal service

5. With regard to the universal service, under condition 12 of its licence Jersey Post is required to deliver mail to every business and residential address on the Island, collect mail from its network and provide an international mail service, six days a week. Such services must be provided at an affordable and uniform tariff across the Island, with preferential rates for literature for service personnel and the blind and partially sighted.

6. The CWU believes that the USO is both socially and economically beneficial for Jersey and provides a highly valued public service. It is high quality, with Jersey Post exceeding the JCRA's targets for domestic and UK mail, and affordable, with all priority local letter and packet prices cheaper than the first class equivalent for Royal Mail. All European letters up to 100g are also cheaper than Royal Mail and Guernsey Post equivalents.[1] However, we believe that the JCRA's licensing decisions will jeopardise this service.

7. For 2009 Jersey Post has reported that its profits fell from £4.3m in 2008, to just under £1m, due to increased costs from Royal Mail, competitive pressure from other jurisdictions, challenges from technology and a declining domestic and traditional mail market. Letter volumes – the core of the USO – reportedly fell by 13% in 2009, 4.5% in 2008 and 7% in 2007. Jersey Post projects a further fall of 9% for 2010.[2]

8. These declines have been offset by increases in bulk export package volumes, with the fulfilment industry representing 60% of the company's revenues.[3] In 2008 Jersey Post estimated that competition in the fulfilment market would reduce its profits by about 50% - over £2m at that time.[4] A similar reduction today would push the company into a loss.

[1] Based on performance figures and prices published in Jersey Post's size-based pricing application, February 2010.
[2] Latest profit and mail volume figures are reported in Jersey Post's press release dated 1/4/2010 responding to the JCRA's decisions concerning Citipost and Hub-Europe (http://www.jerseypost.com/news/Pages/JCRADecision.aspx) and 2008 and 2007 mail volume figures for traditional mail volumes are from Jersey Post report and accounts 2008 and 2007 respectively. The projected decline is from Jersey Post's submission to the JCRA on size based pricing, February 2010.
[3] Jersey Post annual report 2008
[4] Jersey Post Annual Report 2008

9. As the JCRA recognises, profits from this area of the business are used to sustain the USO which itself is a loss making operation for the company. The introduction of competition into this sector, against the backdrop of a 75% fall in profits for 2009 and declining mail volumes, will therefore clearly have a significant impact on the sustainability of the USO in its current form.

10. Jersey Post estimates that the universal service imposes a net cost of around £5m per annum on the business and with the requirement to make collections and deliveries every day, lower mail volumes are not matched by lower costs. We note that Jersey Post had approached the JCRA to discuss altering the universal service obligation in its licence – to providing five deliveries a week rather than six – even before its initial decisions concerning Citipost and Hub-Europe. In addition we note that part of the JCRA's workplan for 2010 is to review the scope of the USO and that the decline in volumes have meant that Jersey Post is making over £1m less than its target revenue set by the JCRA under the current price control.

11. If volumes continue to fall as projected the net cost of the USO is likely to rise in the coming years and if Jersey Post's main revenue stream is reduced the quality, affordability and accessibility of the USO – which the JCRA is obligated to consider – will inevitably suffer. The CWU believe that granting licences to Citipost and Hub-Europe would be the wrong decision for the overwhelming majority of those who use postal services in Jersey.

<u>The JCRA's analysis of the impact on the USO</u>

12. In its initial decisions regarding Citipost and Hub-Europe the JCRA stated that the introduction of competition would not 'result in Jersey Post no longer being able to provide the USO' on the following grounds:

    i. that Jersey Post has sufficient cash reserves to fund the USO even if it lost a significant amount of business;

    ii. that Jersey Post has scope for efficiency savings to contribute towards the cost of the USO;

iii. that the proposed licences do not apply to standard mail, but large letters and packets, and have minimum volume requirements; and

iv. that the JCRA has the discretion to levy Citipost and Hub-Europe to contribute to the cost of the USO.

The CWU does not accept this reasoning.

13. Firstly, as outlined above the CWU believes that the USO will not survive in its current form if the JCRA proceeds with its intention to open up the bulk mail market. The JCRA is obliged to assess whether services meeting current and prospective demand are provided, having regard to the quality, affordability and accessibility of such provision. We believe that this duty is not discharged by asking only whether a USO would still be provided, as the JCRA appears to have done.

14. Furthermore, the CWU disagrees with the four points the JCRA has used to substantiate its argument. With regard to points (i) and (iv) we note that the JCRA and Jersey Post disagree over the current net cost of the USO and there is a gap of at least £4.85m between Jersey Post's estimate of £5m and the last estimate published by the JCRA of £100,000-£150,000 (based on figures from 2007). The difference between these estimates is significant and is equivalent to just under 9% of Jersey Post's total cost of sales for 2008.

15. While the JCRA stated in its initial notices that it has 'carried out significant work with its professional advisers on the cost of providing the USO' this has not been published and the JCRA does not disclose any estimate of this in its decisions. The cost of the USO is clearly germane to any assessment of (1) Jersey Post's ability to provide the service; (2) the reasonableness of such an obligation on the company; and (3) the likely impact of introducing competition. We do not believe the JCRA should have taken such a decision without a clear picture of its implications.

16. Furthermore, in relation to point (i), the CWU is concerned that the JCRA is proceeding with a decision which it envisages could push the publicly owned USO provider into a loss-making position. Relying on Jersey Post's cash

reserves to fund the USO is clearly not a long term or a sustainable solution and jeopardises the future of the service.

17. With regard to point (ii), that Jersey Post 'has scope for efficiency savings which could be used to contribute to the cost of the USO', the CWU is again concerned that the JCRA has not evidenced this.

18. Firstly, the cost of the USO is central to the question of efficiency savings, given that many of the burdens this places on Jersey Post will be relatively fixed and the company will be unable to make savings on these.

19. Secondly, the last efficiency review undertaken by the JCRA was in 2007, when Jersey Post was found to be an 'efficient operator.' The company is on course to meet the target it was set by the JCRA at this time, to make a £2.8m saving in further efficiencies by the end of 2010 and in January, with agreement from the CWU, it commenced on an 80 employee redundancy scheme (equivalent to a 21% reduction in staff on figures for the end of 2008).

20. No comprehensive assessment of the efficiency of Jersey Post has been conducted since 2007 and the JCRA has only recently completed the tendering process for a new efficiency review of the business. It is therefore unclear what evidence the JCRA has for its claim that there is scope for further savings to be made.

21. Finally, on point (iii), while the JCRA decisions would grant Citipost and Hub-Europe licences in the bulk mail sector only, the CWU notes that this is the most profitable part of Jersey Post's business and accounts for over half of its revenue. Additionally, the JCRA has presented no breakdown of the market by letter or packet size to demonstrate the impact of the restrictions within the proposed licences on these criteria. Therefore, for the reasons outlined above we do not believe that the USO will survive in its current form if new licences are granted in this sector.

<u>Quality and affordability of service within the bulk mail market</u>

22. Together with the USO, under article 8 of the Postal Services (Jersey) Law the JCRA is obliged to consider whether other postal services meet current

and prospective demand. While the JCRA cited a survey of eight fulfilment providers in favour of its decision, we do not believe the potential benefits of introducing new licensees in this area outweigh the inevitable costs to the USO or the interests of the majority of postal service users in Jersey.

23. Firstly, as recognised by the JCRA in its consultation regarding Citipost's licence application, Jersey Post already faces competition for fulfilment providers from other jurisdictions including Guernsey and Switzerland – both of which, like Jersey, qualify for the European Union low value consignment VAT relief scheme (discussed in more detail below) – and the UK, where businesses have direct access to Royal Mail's network.

24. Secondly, the bulk mail service provided by Jersey Post is both high quality and competitive. In its 2008 consultation on Jersey Post's quality of service standards the JCRA noted that Jersey Post was considering introducing targets for its bulk mail performance, however the regulator recommended against doing so and stated that Jersey Post's sampling results for January and February of that year showed that 93% of bulk mail deliveries were completed within 3 working days. The consultation went on to note that Jersey Post and Royal Mail agreed on a target of 87% of deliveries to be completed within 3 working days 'based on what Royal Mail feels their network can bear.'

25. Given these factors, the CWU does not believe that introducing domestic competition into the bulk mail market in Jersey will have significant benefits and, moreover, we do not believe that these benefits could outweigh the costs of pushing the USO provider into a loss making position.

The JCRA's secondary obligations

26. Under article 8(2) of the Postal Services Law the JCRA is required to have regard to a number of issues in line with its primary duties. The JCRA's initial decisions regarding Citipost and Hub-Europe focus on two of these: the effect of competition on postal services under article 8(2)(a) and (b); and the JCRA's duty to perform its functions in line with Jersey's economic interests (article 8(2)(c)).

27. In terms of competition, the JCRA states that the benefits for postal users are 'well known', citing the Hooper Report from 2008 to justify this. However the CWU does not believe that this is supported by a holistic view of the evidence or a proper reading of the report.

28. In the UK mail market full competition was introduced in January 2006, following incremental market opening from January 2003. Between 2005 and 2008 while there were some small real terms reductions of between 1-4% in bulk mail prices, there were real term increases in the price of metered mail – of 4% for first class and 2% for second class – and significant rises in stamped mail prices, with first class mail costs rising by 7% and second class mail by 14%.[5] It is clear that in terms of prices the majority of consumers have paid the price for gains of a minority sector of postal users.

29. Alongside these price increases the service provided to the public has declined. Royal Mail moved from two daily deliveries to one in 2004 and ceased Sunday collections in 2007. In parallel to these changes delivery times have become significantly later. In 2003 Royal Mail aimed to complete its first delivery by 9.30am, whereas today it aims to complete its single delivery by 2pm in urban areas and 3pm in rural areas. There are currently proposals to make these times one hour later respectively.

30. The interim report of the Hooper review acknowledged these issues, stating that 'there have been no significant benefits from liberalisation for smaller businesses and domestic consumers' and the final report discusses only the possibility that such groups may benefit in the future. The CWU would therefore question the JCRA's reliance on the report as showing the 'well known benefits' of competition.

31. The Hooper report also estimated that competition had reduced Royal Mail's operating profit by £100m in 2007/08. However, profits for Royal Mail's letters business fell from £344m from 2005/06 to a £3m loss in 2007/08 (full liberalisation of the market took place in January 2006) and the CWU believes that £100m underestimates the true cost of competition to the business. Even

[5] Figures from Royal Mail submission to the Hooper review.

on the more conservative estimate however a £100m reduction represents a fall in profits from 2006 of just under 30%.

32. In 2008 Royal Mail reported that 40% of the bulk mail market had gone to rival mail companies and a similar trend would have serious implications for Jersey Post, in particular given that its profits totalled less than £1m for 2009. The experience in a number of countries like the UK has shown competitors, which do not face the same costs or obligations as incumbent operators, are able to 'cream-skim' by undercutting USO providers' most profitable areas of business, such as the bulk mail market. The CWU therefore does not believe that the reality of competition in postal markets, or its likely impact in Jersey, is adequately reflected in the JCRA's decisions.

33. Furthermore, while we do not accept that competition has been beneficial for UK mail users, it is clear that Jersey Post is not a direct parallel with Royal Mail or many other European operators. While it has a dominant position within Jersey, the market is narrower and less diverse than those in larger countries and Jersey Post's revenue is more concentrated on one sector. This is likely to mean that Jersey Post's ability to withstand competition is even more limited than many other incumbent operators.

34. With regard to Jersey's economic interests, the JCRA's initial decisions state that should the granting of licences to Citipost and Hub-Europe result in lower prices for fulfilment providers Jersey may become more attractive to such businesses. As we have outlined above we are sceptical that such benefits will be delivered, or that they outweigh the costs the decisions would have for the USO.

35. The CWU further notes on this issue that in 2006 the Jersey States issued a policy notice introducing a licensing regime for fulfilment providers on the Island and has since restricted growth in the sector. This has, in part, been a response to pressure from the UK, which is the main market for fulfilment providers based in Jersey.

36. Under European Union law the UK (and other member states) are required to provide VAT relief for low-value consignments of goods imported from outside of the EU. The UK opted to apply the relief to goods worth less than £18,

roughly double the threshold required by the EU and the maximum threshold permitted. For UK Revenue and Customs opting for a higher rate than that required under EU law is a trade off, weighing the lost tax revenue against the extra administrative costs it would face in dealing with a larger volume of goods if the threshold were to be lower.

37. The UK Treasury has supported the current limit as a result of the measures taken in Jersey since 2006, however, at a cost of around £110m[6] to the UK Treasury - £80m of this is estimated to come from the Channel Islands[7] - there is a balance to be struck and the current limit is kept under review. If the number of fulfilment providers in Jersey increased it seems likely – particularly in the current financial climate – that the UK would adopt the lower threshold, or alter the beneficial VAT arrangements for imports it has agreed with Jersey individually[8], to reduce the cost to the UK taxpayer.

38. It is clear from the foregoing that the potential for expanding the fulfilment market in Jersey is restricted and that it is largely dependent on decisions of cost and public finances in the UK. However, the JCRA does not appear to have recognised these constraints in predicting that granting licences to new bulk mail providers could cause the market to grow.

39. In terms of assessing the economic impact of the JCRA's initial decisions, we would also submit that the impact on the USO must be taken into account – something the JCRA has failed to do. The USO and Jersey Post serve businesses across the Island and increases in standard mail prices or a reduction in the service, which we believe are the likely consequences of introducing competition into the bulk mail market, will have a detrimental effect on the wider competitiveness of the Jersey economy. As we have noted above, the experience in the UK is that the majority of postal users have paid the price for liberalisation and the CWU does not believe that the economic issues the JCRA has raised in its initial decisions reflect the impact this would have on Jersey's overall competitiveness.

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[6] The figure was given by Stephen Timms, then Financial Secretary to the Treasury, in a Westminster Hall debate on the low-value consignment VAT relief on 27/1/2009.
[7] This amount was given by Stephen Timms in response to a written question on 12/2/2009.
[8] As discussed in the submission to the JCRA from Jersey Customs in its consultation on Citipost's licence application there is a memorandum of understanding between UK HMRC, Jersey Post and Royal Mail, which allows for the collection of UK VAT in Jersey enabling imports to circumvent UK customs controls.

40. Finally, the CWU notes that Citipost will not be based in Jersey and will therefore not be paying tax and will have a limited commitment in terms of employment on the Island. In light of the arguments above, we believe this adds to the clear net-cost the JCRA's decisions would have for the Jersey economy.

Conclusion

41. The CWU is clear that the introduction of competition should remain subordinate to maintaining a viable universal service and we believe that this priority is reflected in the JCRA's statutory duties. However, its initial decisions to grant licences to Citipost and Hub-Europe are not in line with this obligation and will jeopardise the future of the USO.

42. We are concerned that the JCRA's decisions will push Jersey Post into an unsustainable position and that they have been made without a proper assessment of the impact, in part due to a lack of information on the costs of the USO or the efficiency of Jersey Post. We also believe that the JCRA has misdirected itself in asking only whether a universal service will survive, and not whether the service which remains will meet the needs of the majority of postal users on the Island.

43. The CWU does not agree with the JCRA's assessments of the potential benefits that competition may bring – on the measures under both its primary and secondary duties – and, in particular, we are concerned that these have been given undue weight against the costs the overwhelming majority of postal users will face. We would therefore urge the JCRA to reconsider its decisions.

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