CWU RESEARCH

Submission to the JCRA – initial notice for the proposed grant of a postal licence to TNT Post UK Ltd

The Communication Workers Union (CWU) represents 215,000 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.

We welcome the opportunity to comment on the Jersey Competition and Regulatory Authority's (JCRA) initial notice proposing to grant a licence to TNT Post UK Ltd (TNT). In the initial notice the JCRA outlines its view that the proposal is in line with its duties under the Postal Services (Jersey) Law 2004.

The CWU disagrees with this position and in repeated submissions to the JCRA we have outlined our opposition to the liberalisation of the postal market in Jersey in the current climate, on the grounds that this is inconsistent with the survival of the universal postal service, which the JCRA is duty-bound to safeguard. We regret that the JCRA has decided to introduce competition into the Jersey bulk letters market from 2011 and the bulk packets market from 2012, with its final decision to grant licences to Citipost and Hub Europe published in October 2010.

We believe that granting a similar licence to TNT, over and above this, puts the future of Jersey Post and the universal service in further jeopardy. Not only do we have concerns about increasing competition *per se*, but we believe the award of a licence to such a large operator, into a market with little potential for growth, is likely to be particularly damaging to postal services on the Island. We believe that moves are already being made to cut the universal service from 2011.

We therefore disagree with the JCRA that the award of a licence to TNT would be in line with its primary duty and, as with its previous decisions, we are seriously concerned over the absence of evidence from the JCRA to substantiate its claims regarding the impact of its proposals. The JCRA has acknowledged that it has not taken account of £500,000 in annual payments by Jersey Post to meet its pension deficit and we do not believe that it has properly assessed the consequences of liberalisation.

Furthermore, we do not agree with the JCRA's claims that the introduction of competition will have broader economic benefits for the Island or postal users as a whole. While such aims are subject to its duty to safeguard the universal service, we do not believe the evidence relating to these supports the JCRA's position. The CWU therefore urges the JCRA to reverse its decision and to undertake an urgent review into its plans to liberalise the postal market in Jersey.

The JCRA's primary duty

Under article 8(1)(a) of the Postal Services Law the JCRA's primary duty is to ensure that postal services which satisfy all current and prospective demand are provided within Jersey. Under guidance from the Economic Development Committee issued in 2005 this includes ensuring the provision of a universal postal service five days a week. Jersey Post's current licence requires it to do so six days a week.

As we have outlined in previous submissions to the JCRA we believe that the introduction of competition is inconsistent with the maintenance of the universal service. In 2009 Jersey Post reported an operating profit after tax of £230,000 – a fall of 96% on the previous year – and, even without the introduction of competition in Jersey, the company is projecting being pushed into an unsustainable loss in the coming years on the back of a forecasted decline in mail volumes.[1]

In response to this the CWU has signed up to a programme of fundamental change to deliver cost savings of £4.9m by the end of 2011 with a voluntary redundancy programme for over a fifth of staff on 2008 levels and the introduction of a new grade and a skills mix project, which will see around a third of our members moving onto lower pay rates. We do not believe that there is scope for the business to go further, or that any other business or government department in Jersey is undergoing change on this level.

The introduction of competition, over and above the projected trend in volumes, will have a significant impact on the business. In 2008 Jersey Post estimated that the

[1] Jersey Post has predicted that letter volumes for 2010 will be down by 9% on 2009.

introduction of competition in the fulfilment industry would reduce its profits by around 50% - between £2m-£3m at that time.[2] Against current profit levels, even with successful delivery of the efficiency programme, a loss at the lower end of this scale would simply be unsustainable for Jersey Post and we believe the universal service will be sacrificed as a result.

It is clear that this trade off is taking place. In 2009, while liberalisation of the bulk mail market was under consideration, Jersey Post approached the JCRA with an application to reduce the universal service obligation (USO) to five days a week and the JCRA's Strategic Plan for 2011-13 includes amending Jersey Post's licence 'to reflect any changes to the universal service obligation' in the second quarter of next year. In its final decision to grant licences to Citipost and Hub Europe the JCRA openly discusses reducing the USO to save costs, in light of concerns over the impact of competition for the future funding of the service.

We also note that the Minister for Economic Development has also signalled he would accept a reduction from the current six day provision to a five day service each week, though only where 'all possible alternative remedies have been attempted.'[3]

The Minister and the JCRA have sought to deny the role of competition in this process: the States consultation on the USO in June 2010 stated that the impact of competition would only 'accelerate what would already happen' and this reasoning has been echoed by the JCRA, which has stated 'with or without competition…the current operations of [Jersey Post] are in need of review.'[4] However, it is hard to understand how the introduction of competition into its most important market – taking away millions of pounds worth of revenue, which it is far from inevitable that it would otherwise lose to international competitors – would not independently damage the company and its ability to sustain a loss-making service.

In its initial notice regarding TNT's application the JCRA also asserts that the universal service will not need cross-subsidisation from bulk mail following Jersey Post's efficiency programme. However, we understand that Jersey Post disputes this

[2] Jersey Post Annual Report 2008. It is not clear whether the estimated impact of competition in Jersey related to operating profit (£4.3m) or total profit before taxation (almost £6m).
[3] Postal Services in Jersey: Consultation on the Universal Service Obligation, 23rd November 2010.
[4] The JCRA's final decision granting licences to Citipost and Hub Europe, 8th October 2010.

assessment and we do not believe that it accurately reflects the finances underlying either the business or the USO.

We note that the JCRA's last published estimate of the cost of the USO was £4.85m less than the current estimate from Jersey Post and that the JCRA has acknowledged that its analysis does not take account of £500,000 of annual payments from Jersey Post to meet its pension deficit. We are also concerned that the JCRA has not produced any evidence to substantiate its claim and that it has still not completed or published its updated efficiency review of the business, its statistical review of the postal and logistics market or an updated assessment of the cost of the USO. We believe each of these should have been completed before the JCRA could properly understand the impact of its proposals.

We are strongly opposed to a reduction in the USO which we believe its decisions will bring about and note that neither the States consultation, nor the JCRA have sought views on downgrading the service to five days a week. While we disagree with the analysis presented to respondents in the States consultation document, which downplayed the role of competition in cutting the universal service, the results clearly provide no mandate for changing the universal service. Furthermore, the union's petition against reducing the universal service was signed by over 3,000 members of the public over the summer; more than six times the number of responses received to the consultation.[5]

We believe that even more radical cuts to the USO, than a reduction to a five day service, will be brought in in the future as a result of competition. The fulfilment market provides 60% of its revenue and with mail volumes being forecast to decline over coming years the costs of the universal service will rise. It is inevitable that Jersey Post will look to reduce these further, as it is already seeking to do, as its revenue from profitable areas of the business fall.

The JCRA's initial decision suggests two ways it believes the USO can be funded in such a scenario. Firstly it states that Jersey Post could fund the service from cash

[5] The petition stated: After the recent consultation paper from the Economic Development Department, the people of Jersey feel that the States should fund Jersey Post so that it can maintain the level of delivery of mail on the Island. Furthermore we feel that the States should intervene on behalf of the people before we lose our postal service, as we know it, forever! We also feel that the states should find alternatives to redundancies in Jersey Post before we are left with an large increase to the already high unemployment levels.

reserves. However, it is clear that this would be unsustainable going forward and push the company into insolvency and, furthermore, its assessment that Jersey Post can meet a loss – which it anticipates arising over the next two years – from its cash reserves only runs until 2012. This is not a long term solution.

Secondly, it discusses the potential to levy other operators for a USO compensation fund. We note, however, that there is political opposition to this, with the Minister for Economic Development stating that the USO should be self-financing and that it should not be funded by other operators. Such a move would also be strongly opposed by competitors and we are sceptical that the JCRA would force this through. In the Green Paper published in November on the USO the Minister stated that the JCRA must exhaust all other options before downgrading the USO but we note that the regulator is discussing changing the universal service, without mentioning this mechanism, in 2011.

As stated above, while we oppose the introduction of competition at the current time *per se*, we are particularly concerned over the proposal to grant a licence to TNT, a far larger operator than any of those licensed in Jersey. Its UK arm alone has a turnover over five times greater than Jersey Post in its entirety and, as such, there is a real risk it will quickly become dominant in such a small market and squeeze out other postal providers. This is a particular risk given the limited potential for growth in fulfilment in Jersey, given tax issues, as discussed below.

We are also concerned that the JCRA has made no specific assessment of the impact of such a significant operator entering the Jersey postal market or of the level of competition which it considers to be either necessary, or which would not have negative consequences for the broader market. We believe that this is a mistake and that a full impact assessment of the specific decision to grant a licence to TNT needs to take place.

<u>The JCRA's secondary duties</u>

Under article 8(2) of the Postal Services Law the JCRA comes under a number of secondary duties, subject to its primary duty under article 8(1). Two of these are highlighted in the initial decision regarding TNT.

Under article 8(2)(a) the JCRA has a duty to perform its functions to protect and further the short and long term interests of users of postal services, by promoting competition where appropriate. However, as with its decisions to grant licences to Citipost and Hub Europe, we believe that the JCRA overstated the potential benefits to users.

Firstly, Jersey Post already faces competition in this sector from other jurisdictions including Guernsey and Switzerland – both of which qualify for the European Union low value consignment relief scheme – and the UK, where businesses have direct access to Royal Mail's network.

Tesco recently relocated its fulfilment business from Jersey to Guernsey and the CWU understand that Jersey Post has lowered its prices to keep its business with Play.com, which had been in discussions with Swiss mail companies. It is clear from this that Jersey Post already faces competitive pressures requiring it to provide an efficient cost-effective service to fulfilment providers.

Secondly, reflecting this, the bulk mail service provided by Jersey Post is both high quality and competitive. The regulator has acknowledged that Jersey Post has outperformed its targets for bulk mail and that the requirement for 87% of deliveries to be completed within 3 working days – as opposed to 93% which it was achieving in 2008 – on the basis of what *Royal Mail* felt *their* network could bear.[6]

Thirdly, in its last review of the business in 2007, the JCRA acknowledged that Jersey Post was an efficient operator and set the company a target of making £2.8m further savings by the end of 2010, which the business is on course to meet. Jersey Post has announced further plans to make efficiency savings beyond this and with an operating profit margin of only 1.4% in 2009 it is far from clear that the company is not offering fulfilment providers value for money.

We also note that that the JCRA is again relying upon the Hooper review in stating that 'the benefits of competition…are well known.' As we have previously outlined we believe that this is a misreading of the reports and that it fails to take account of the reductions in service and greater increases in cost which the majority of users have faced. Furthermore, the updated review notes that the 'overarching question' today is

[6] JCRA Consultation on Jersey Post's quality of service standards 2008.

the point at which protecting the universal service comes into direct conflict with promoting competition and goes on to quote the 2008 Hooper report, stating: 'competition reduces Royal Mail's revenue available to support the universal service.' We regret that the JCRA has overlooked this.

The JCRA has also suggested that the introduction of competition is in the economic interests of the Island as a whole, in line with its duty under article 8(2)(c). However, we believe it directly jeopardises this. As we have argued previously there is limited potential for growth in the fulfilment market in Jersey, given that its primary attraction is the low value-consignment relief scheme, the continuation of which at its current level comes at a cost to the UK taxpayer is subject to economic considerations of the UK Government.

With the cost to the UK – attributable to the Channel Islands – of the current arrangement estimated to be around £80m, this is now being 'actively reviewed' and the recent dispute over Jersey's 'zero/ten' tax regime for corporations emphasises that the future of this is in a precarious position. We therefore disagree with the JCRA that introducing competition into the bulk mail market could attract new fulfilment companies to the Island.

Finally, we note that the JCRA is under a duty to have regard to the special needs of persons who are disabled, have limited financial resources or other special needs under article 8(2)(e). The JCRA asserts that the proposed licence is 'neutral' in this regard. However, we believe the risks to the universal service has direct consequences for vulnerable groups, who were highlighted in the States consultation on the USO as being particularly dependent on the current postal service which guards against social exclusion and marginalisation. The JCRA needs to consider their needs and not simply focus on potential benefits competition may bring for a minority of bulk mailers on the Island.

Conclusion

The CWU strongly opposes the further liberalisation of the bulk mail market being proposed by the JCRA. As we have stated we believe a direct trade-off is being made between the maintenance of the current universal service and the introduction of competition and that the ground has already been laid for this for 2011.

We are concerned that the JCRA is ignoring genuine costs on the business and that it has not substantiated its assessment of the prospects for the universal service going forward, against a background of declining volumes and its proposed liberalisation. We also believe that the JCRA needs to specifically consider the costs of granting a licence to a significant player, such as TNT, which has far greater resources than other providers in Jersey, and could quickly become a dominant player, hitting the USO, Jersey Post and other operators alike.

The JCRA must now take a step back and review its proposals for liberalising the bulk mail market and we would urge it to reverse its initial decision regarding TNT.

For further information please contact:

Peter Donaghy
Vice Chair of the Postal Executive
Communication Workers Union
150 The Broadway
London
SW19 1RX

Tel: 020 8971 7598
Email: pdonaghy@cwu.org

RD10/12/137
23rd December 2010