

ANNEX B: ROYAL MAIL'S RESPONSE TO POSTCOMM'S SIXTEEN ISSUES IN THE CONSULTATION ON THE UNIVERSAL SERVICE

The appendix below responds to the specific sixteen issues raised by Postcomm in chapter 6 of the consultation document. Postcomm's questions are quoted in italics. Royal Mail's responses are outlined briefly with references to the main body of the text where a fuller answer is supplied.

(1) Chapter 2 considered the concept of a universal postal service and identified the essential elements of such a service as being open to everyone, everything, everywhere, noting that in the UK there are the additional requirements of an everyday service and a geographically uniform tariff.

Issue 1: Does this sum up the essential elements of the universal service? Are there any other elements which should be included as essential features of a universal postal service?

[See section 3 of Royal Mail's response] Royal Mail endorses this framework as providing a useful description of the essential elements of the USO with two exceptions. First, the definition of universal postal services should be explicitly restricted to *postal* services rather than add-on features. Second, the interpretation of the "uniform tariff" should be modified to allow prices that vary by destination while the tariff for any given destination would remain uniform for all senders throughout the country. Beyond this, Royal Mail does not consider that there are any further elements that require adding to the proposed definition of the universal service.

(2) Chapter 3 put forward an analytical framework for identifying the different types of postal services and suggested four kinds of basic postal services: priority, non-priority, economy and a secured service.

Issue 2: Do you agree with this categorisation of four basic postal services? Are there other types of postal services that should be considered in this analysis?

Royal Mail endorses this framework for categorizing postal services, although Royal Mail does not consider that there needs to be a universal service product in each category. In particular, the universal service may not include an economy product owing to Royal Mail's recommended exclusion of Mailsort 3 [see section 4]. In fact, the core of the universal service is priority mail alone, since first class drives the costs of both the extensive upstream network and delivery costs through the requirement to deliver six days a week.

(3) Issue 3: Should the universal service be seen, in conceptual terms, as a comprehensive range of postal services that meet a variety of customer needs or as a more limited range of services that meet the basic needs of customers? Whatever view you take on this issue, which of the four (or more) types of basic postal service do you think should be regarded as part of the universal postal service?

[See section 4] The requirements of the universal service are clearly laid out in the PSD and the PSA. To fulfill these requirements Royal Mail proposes providing stamped and metered first and second class products, a registered Special Delivery product and a Standard Parcel product. This implies that the universal service will consist of a priority service (first class), two non-priority services (second class and Standard Parcel) and a secure priority service (Special Delivery). Cleanmail will be offered as a generic bulk mail product in order to keep a bulk mail product within the USO. Postcomm's proposed framework, while useful for categorizing postal services, does not have any direct relevance to defining the universal service.

(4) Issue 4: Should any changes to the requirements of the universal service be made now – or should they be introduced over time as competition becomes established?

The current interpretation of a “uniform tariff” should be modified now to allow tariffs to vary by destination cost-reflectively while the tariff for any given destination would remain uniform for all senders throughout the country, allowing Royal Mail to compete effectively as competition develops and avoid the growth of inefficient competitors exploiting cream skimming opportunities. Equally, Postcomm should consider recommending the relaxation of the operational restrictions of the USO (for example, high density of pillar boxes, 6-days-a-week delivery) to reduce the burden on Royal Mail as competition develops.

(5 and 6) Chapter 4 identifies the key implications of the different ways of regarding the universal postal service:

(i) the universal service requirement for daily collection and delivery of mail to every address in the UK

(ii) the requirement that prices of universal services are geographically uniform in the UK

(iii) the possibility that these requirements may impose a cost

(iv) the fact that these requirements constitute a regulatory impact on the universal service provider

(v) the wider impact that the universal service has in determining the scope of the regulatory framework, including Postcomm's ability to safeguard the universal service through licensing

Issue 5: Are there other regulatory implications which Postcomm should have in mind in considering what services should be taken to constitute the universal service in the UK?

Royal Mail identifies three key regulatory implications of the definition of the universal service:

- **The opportunities created by a national uniform tariff for cream skimming:** the cross-subsidies inherent in the maintenance of the current uniform tariff create opportunities for cream skimming. For example, competitors can undercut the national uniform tariff by delivering only urban mail, which is substantially less expensive to deliver than rural mail, either not taking, or re-posting, the remaining mail. Furthermore, if they also have access to Royal Mail's delivery capability at a national uniform price, this then provides a lower cost route to dispose of costly-to-deliver mail, further subsidising cream skimming entry.
- **The operational burdens imposed by the USO requirements:** beyond facilitating cream skimming by competitors, the universal service imposes additional operational burdens on Royal Mail (for example, the requirement to deliver letters six days a week, maintain a high density of pillar boxes, and to deliver to each individual residence's door) which it would not incur voluntarily even if it provided a five day, next day service to everyone, everywhere. The fact that competitors will not under Postcomm's liberalisation programme bear any USO requirements allows competitors to deliver second and third class mail only once or twice per week on a given walk, potentially reducing their costs substantially below those of Royal Mail.
- **The need to maintain Postcomm's licensing powers:** the Postal Services Regulations of December 2002 – which were enacted to implement the amended European Postal Directive – introduce the distinction between the USO and the scope of the USO, with a product being within the scope of the USO either if it is within the USO or if it is sufficiently similar to a USO product. Any product within the scope of the USO requires a licence, so allowing Postcomm to manage the liberalisation process for products that lie outside the USO itself but still within the scope of the USO. However, those products and services that lie outside both the USO and the scope of the USO are beyond Postcomm's licensing authority and so are effectively fully liberalised, with the result that competition could develop ahead of Postcomm's intended programme and potentially threaten Royal Mail's ability to fund the universal service.

Issue 6: What is the relevance or significance of each of the regulatory impacts or effects described in Chapter 4? What weight should Postcomm place on each of these (and any others that you identify)?

The relevance and significance of the regulatory impacts recognized by Royal Mail is as follows:

- **The opportunities created for cream skimming** form a major threat to the continued provision of the universal service by Royal Mail. It is of utmost importance that Postcomm provides Royal Mail with the flexibility to price postpaid mail cost-reflectively on a geographic basis, so discouraging

inefficient, cream skimming urban entry but allowing efficient rural and urban entry and supporting the long term viability of the USO. Such a provision would be consistent with the need for Royal Mail to have the ability to respond to commercial challenges recognised in the 1999 White Paper.

- **The operational burdens imposed by the USO** comprise another commercial disadvantage to Royal Mail that is not shared by new entrants to the industry, and which jeopardizes the ability of Royal Mail to continue to provide the universal service. Postcomm should therefore consider recommending the relaxation of these operational restrictions to reduce the burden of the universal service as competition develops.
- **The need to maintain Postcomm's licensing powers** requires that Postcomm ensures that those products that are excluded from the universal service remain within the scope of the USO. This will enable Postcomm to manage the introduction of competition in a measured fashion according to the accepted schedule for liberalisation.

(7) Chapter 5 applies the analytical framework and concepts described in Chapters 2 and 3 to Royal Mail's current provision of services to help illustrate some specific issues raised for consideration:

***Issue 7:** How important is it that people should be able to have a choice between 1st and 2nd class mail services? Is this position likely to change as competition develops and as alternatives become available (as seems to have happened for parcels)?*

The British public is accustomed to having a choice between priority and non-priority services, and Royal Mail proposes to continue to provide services to meet this need for choice.

*(8) **Issue 8:** In relation to the requirement for a universal service for parcels, is Royal Mail's standard parcel service a sufficient universal service offering? Should there be a requirement for a faster universal parcels service (see also next issue concerning 1st class post)?*

Given the context of the competitive parcels market, Royal Mail's Standard Parcel service is a sufficient universal service offering as it fulfils all of the essential elements as defined by Postcomm. The Standard Parcel service is available to all, it is collected and delivered everywhere on a daily basis, and is priced on a geographically uniform basis. It guarantees a minimal parcel service for all mail users throughout the UK. A faster universal parcels service is offered by Royal Mail under its first class product, while Parcelforce and other parcels and express operators offer a full range of postal and add-on services for express parcels. There is therefore no need for further fast parcels services.

(9) Issue 9: Can 1st class post (which technically handles parcels as well as letters) be properly regarded as a fast universal service for parcels, given its current level of charges for higher weight items?

The express parcels market provides a clear example of the fact that while the universal service provides a limited service, the market can be relied upon to provide a more comprehensive one. First class post fulfils all the essential elements identified by Postcomm as defining the universal service. However, as Postcomm observes, at higher weight steps using first class post for parcels is relatively expensive. The parcels market is, of course, fully liberalized, and as a result customers have the choice of using Parcelforce or another parcels' operator, who offer lower cost services at this weight level. Furthermore, as a result of the competitive impetus, parcels' operators also offer many value-added services, such as track and trace capabilities. In this way, while first class guarantees a limited level of service to everyone, everywhere, competitors provide a range of priority parcels services.

(10) Issue 10: Where Royal Mail has a number of product variants of the same service, do they all need to be required to be provided as part of the universal service? For example, should Royal Mail be required to provide a full range of bulkmail products (e.g. Mailsort, Walksort, Flatsort, Cleanmail) as part of its universal service or just some of them ?

[See section 5] Royal Mail should not be required to provide a full range of all products and services as part of the universal service. The universal service guarantees a limited standard of postal service to all users; not the provision of a comprehensive selection of services. Moreover, bulk mail services are not available to everyone for reasons of the operational and volume requirements to meet the necessary acceptance criteria. These products should therefore be removed from the universal service (unless zonally differentiated pricing will be permitted within the universal service), while remaining within the scope of the USO. To fulfill the need for a universal service bulk mail product, Royal Mail proposes creating a new Cleanmail product that will be priced at a uniform national rate, have only simple operational criteria and so be available to all users.

(11) Issue 11: Should the universal service include a requirement on Royal Mail to provide a specialised newspaper service – i.e. should Presstream 1 and 2 which are only available to certain types of users and cover only newspapers and magazines be treated as part of the universal service?

[See section 5] The universal service should not include Presstream 1 and 2 as they do not conform to three of Postcomm's essential elements for defining a universal service. They are available, as Postcomm observes, only to certain types of user, i.e. those in the publishing industry. They do not cover 'everything' as they provide a service only for the delivery of newspapers and magazines.

(12) Issue 12: Should an economy mail service (in Royal Mail's case this is Mailsort 3) which is a seven day delivery service and only available to large mailers in respect of certain types of mail be treated as a universal service? Should such a service be available to users generally ?

[See section 5] Since Mailsort 3 is not available to everyone and does not require a delivery every working day it would appear to fail Postcomm's test for a universal service. There is, therefore, no existing postal service that can satisfy Postcomm's criteria for an "Economy post" universal service at a price and standard of service below that of second class. However, Mailsort 3 should remain within the scope of the USO on account of its operational similarities to the generic universal service bulk mail product. This will enable Postcomm to ensure a managed transition to liberalization for the economy postal service market.

(13) Issue 13: Do the basic tariff services for letters and parcels in international mail provision adequately meet the requirements for a universal postal service?

The basic tariff services for international letters and parcels do indeed fulfil the requirements for a universal service as they provide a service that adheres to the essential elements outlined by Postcomm for an everyday service, everywhere, available to everyone. However, international services provide an important example of prices that are not geographically uniform as traditionally interpreted but vary in way which broadly reflects delivery costs, in this instance terminal dues.

(14) Issue 14: Are there any "add-on services" such as "Redirection" or "Keepsafe" which should be provided on a universal service basis (such as the redirection service) or should these be regarded as services that are provided as best practice by Royal Mail?

[See sections 3 and 5] The definition of universal postal services should be explicitly restricted to **postal** services. Add-on features to a postal service which are not in themselves postal (i.e. do not consist of the collection, processing, transporting and delivery of postal items) should not, therefore, be classified as an element of a universal postal service. Any provision of such features by Royal Mail should be regarded as a response to customer demand rather than regulatory obligation. However, associated postal services which provide for the forwarding, redirection and retention of mail items should be included within the universal service obligation.

(15) Issue 15: Should Royal Mail's services that provide downstream access to its postal facilities be considered as part of the universal service?

[See section 5] Postcomm is currently consulting on the access prices that will be provided to UK Mail, and Royal Mail does not consider it appropriate to comment on the universal service status of access until the outcome of the consultation is known.

(16) Issue 16: In considering what services should constitute the universal service are there any other issues that you think are relevant ?

For a full discussion of Royal Mail's proposals for the universal service, the reader should consult the full text of Royal Mail's response to Postcomm's consultation document.