

STATES OF JERSEY

Economic Affairs Scrutiny Panel Jersey Post and Competition Sub-Panel

TUESDAY, 31st AUGUST 2010

Panel:

Deputy D.J.A. Wimberley of St. Mary (Chairman)

Deputy M. Tadier of St. Brelade

Witnesses:

Mr Mike Liston, Chairman of Jersey Post

Mr Ian Carr, Chief Executive of Jersey Post

[10:02]

Deputy D.J.A. Wimberley of St. Mary (Chairman):

Shall we start formally? It is 10.02 a.m. and the first thing we do is we give our names for the tape so the transcribers know what is what and who is talking when. My name is Daniel Wimberley; I am chairing this in the absence of Shona Pitman and I will explain that later.

Deputy M. Tadier of St. Brelade:

I am Deputy Montford Tadier of St. Brelade.

Chairman, Jersey Post:

I am the Chairman of Jersey Post.

Chief Executive, Jersey Post:

Chief Executive of Jersey Post.

The Deputy of St. Mary:

Okay, and our Scrutiny Officer, Tim, is busy helping us. Right. Well, welcome and thank you for coming. I know you are busy. I think the timing is until 12.00, is that correct? If we need that amount of time.

Chairman, Jersey Post:

We have got another meeting, but this will take precedence. It is a board meeting of Jersey Post.

The Deputy of St. Mary:

Right. You would like to be away ...

Chairman, Jersey Post:

It can wait.

The Deputy of St. Mary:

It can wait? Okay, right. Yes, Shona is our Chairman of this Sub-Panel, it is the Sub-Panel of Economic Affairs. So Monty is not on Economic Affairs, but he has kindly agreed to be on the panel, but Shona has had a bereavement, so she is not able to chair this hearing. There is a document in front of you, which maybe you should read, unless you have read it before. If you read it it sort of gives you various immunities, I think, at a hearing. The hearing is transcribed. You will get a copy for verification of whether it is a correct record or not, or if they have misspelt anything, which they sometimes do. Is that everything covered? Right. Okay, so Monty, do you want to kick off? Well, no, first of all I will outline where we are going to try and keep to in terms of an agenda. We are going to talk about competition, the principle of it and the principles of cross-subsidy and how that fits and whether you are entitled to do that and so on. So we will look at that. We will also look at the specific issues around the competitors and what they are saying about you and what you are saying about them because there are some quite interesting issues there. Profitability and efficiency: so we will look at all that and how you have achieved that and where you think that is going because obviously there is a challenge there as well to you; the relationship with the States, the various Ministers and the J.C.R.A. (Jersey Competition Regulatory Authority) and how those things pan out. So that is roughly the agenda; we will try and stick to it so you know what things are coming and when they are coming and then other matters. So, Monty, do you want to kick off with competition?

Deputy M. Tadier:

Just to put the first 2 questions in context, we were discussing at the last meeting between ourselves whether semantically it is better to talk about, or more correct to talk about, an increase in competition for Jersey Post or the introduction of competition. So could you tell us what competition exists currently that you already have to deal with in the market?

Chief Executive, Jersey Post:

Competition for Jersey Post is in two forms: the first one clearly is alternative technologies, which you will have seen from some of the data we presented in terms of declining mail volumes; it is a massive competitor to the traditional postal products. The second, as you suggest, is alternative operators physically operating and delivering mail in the Island. At the moment there are two other licensed operators in the licensable area: one being Regency Logistics who have a licence for inbound deliveries and the licence was granted by the J.C.R.A. really to allow the delivery of anything from a letter up to a packet. It is an extension of a contract that operates in the U.K. (United Kingdom) called the DX Service. They deliver to a number of businesses that are in this closed loop in the U.K. The scope of it is slightly limited and it is quite bizarre the way the J.C.R.A. constructed the licence: the scope of the licence is limited by the type of aircraft they can fly the product into the Island.

The Deputy of St. Mary:

I had not expected you to say that.

Chief Executive, Jersey Post:

Well, they did and it is quite bizarre the way it is constructed, but anyway. I think it is fair to add the principle of that particular activity, or part of the activity, was already being undertaken when Jersey Post was incorporated, so there was a fair bit of legitimisation by the J.C.R.A., if you like, of an activity that was already undertaken, albeit that to our knowledge has grown slightly. The other operator in the marketplace at the moment is High Speed Freight, who have a licence for outbound export mail, generally international. High Speed Freight really is a 'frontend' for DHL Global Mail; they run the agency for them on the Island. Their licence was first issued with ... the cap on that

licence was £150,000 per annum in terms of income against outbound international traffic. That has been reviewed and raised; I believe the latest cap is £300,000 a year. The challenge with it is ... I think because people like DHL have direct access into the international mail markets they charge half of what we do for a letter to Australia because they do not have the U.S.O. (universal service obligation) costs sitting around it. The discussions we have with the J.C.R.A., when you calculate the £150,000, the impact on Jersey Post is probably twice that. I think for us we have ... the discussion we have just had recently with the J.C.R.A., we have seen a downturn in our outbound international letter mail volumes of nearly 22 per cent in the last 2 or 3 years, which is quite staggering. So those are the 2 physical operators that ...

Chairman, Jersey Post:

In the courier industry?

Chief Executive, Jersey Post:

Yes, outside of that, of course, anything over £1.35 or 500 grams, we have got ... the courier industry already operates; you have got logistics operators that are out there delivering parcels and despatching parcels outside of the licensable areas. But again, the product that Jersey Post works with, even though it is outside of the licensable area.

The Deputy of St. Mary:

So there is no restriction on those and there never has been?

Chief Executive, Jersey Post:

No, they were formally regulated by the Postal Committee. It used to be the States kind of self-regulating itself and I think back through the years and there is ... probably 12, 13 or 14 years ago, the Postal Committee at the time legitimised or licensed in some form, and it would not have been like they licence now, their courier operators because the Postal Committee, for all intents and purposes, was the regulatory body, if you like, of the postal service in those days.

Chairman, Jersey Post:

Then in the broader context of this hearing on this issue, the real competition that we see, in terms of its impact on our own behaviour, is the competition from off-Island postal operators who are competing to try to attract the fulfilment business away from Jersey principally and Switzerland and the other offshore centres. Also postal operators who offer alternative models for local businesses, in particular the finance industry, to do their postings via the U.K. through a quirk of a pricing mechanism, which makes it ostensibly attractive. So, to the extent to which that impacts on our pricing behaviour, is that - and it will come out later, no doubt - the pricing control that J.C.R.A. has imposed on Jersey Post having done its efficiency reviews, its price control reviews and all the rest of it, we have never got anywhere near charging that price because if we did we would lose a lot of the business mailings to other operators outside of Jersey. So although they are not present in this jurisdiction, they have an impact on our behaviours which are the same impacts that there would be on our competitive behaviour were they in this jurisdiction.

The Deputy of St. Mary:

Right. So you are saying that this business of sending postings to the U.K. and getting them done from there has a direct impact on the business just because that possibility is there?

Chairman, Jersey Post:

Yes. It is a leverage that the larger business users exploit regularly.

The Deputy of St. Mary:

When you say: "Ostensibly attractive", do you mean that ... what do you mean by that?

Chairman, Jersey Post:

Well, the headline rate is slightly under ours, is it not?

Chief Executive, Jersey Post:

The attraction to the business customers is more around ... what they tend to do is to move their database to the U.K. and Royal Mail has a product in the U.K. called downstream access, which what happens is a small company in Jersey will move its data across into a mailing house. That

mailing house will consolidate with a number of other products and that mailing house has a downstream access agreement with Royal Mail. That downstream access agreement, the minimum access price is 13 pence for that. That will not be passed directly on to the customer, but it is going to be an extremely low price. Now, the downstream access agreement, or the condition 9 access agreement, which is a very hefty document in the U.K., allows anybody accessing that Royal Mail downstream access up to 1 per cent of the volume to come to the islands. Now, their pricing, they pay us more than 13 pence, but their pricing model built in for that 1 per cent. But what we have seen probably over the last 5 years I guess is a real upsurge of our inbound volume that comes into the Island now as DSA mail. This is a combination of U.K.-based customers accessing this downstream access product and some of our customers ... we have had a real challenge from the utilities lately, who have been courted by U.K. mailing houses. It represents probably about 25 per cent of the total letter mail volume that arrives every morning on the early morning charter aircraft. So it is a significant product. As Mike was saying, we have seen a huge migration of locally-based customers who send their data across to the U.K., have it compiled into the U.K., and delivered back into the Island.

The Deputy of St. Mary:

So you have got local customers posting mail to local ... you have got local businesses posting mass mailings to local customers, all done in the U.K.?

Chief Executive, Jersey Post:

Yes. The only piece we recover from that is the delivery price that Royal Mail pays us; whereas in a postal infrastructure you would charge a price for that product which also caters for your collection network, your upstream activities, your indoor processing activities. So you are losing that piece.

The Deputy of St. Mary:

You lose the volume?

Chief Executive, Jersey Post:

Yes. Which I think is ... I mean, the whole downstream access arrangement, if we look at Royal

Mail, it has been an absolute challenge for Royal Mail in terms of so many customers have switched their upstream activities to competitors. Royal Mail now have an upstream activity that is not funded. That is a real challenge for them because they never forecast the volumes they were going to make. So a much smaller scale for us, but a similar concept that says: “When those customers choose to switch to the downstream access agreement a competitor gets the upstream part of that income.”

The Deputy of St. Mary:

Yes, but it is really attractive. I mean, it is ostensibly attractive so you are implying that somehow you could get that business back, but you cannot because it really is cheaper.

Chief Executive, Jersey Post:

We would struggle to get that business back, absolutely. It is the Chairman’s point entirely; you know our pricing is so price sensitive, but it is that balance then because you have got such a huge fixed-cost infrastructure on the Island to maintain that delivery service of revenue against cost.

The Deputy of St. Mary:

Okay. Is there any more on competition or the local framework? I have got one more question on where we are now, which is ... or where we have got to. You said 12 or 13 years ago the Postal Committee legitimised the various courier operators who are delivering post, or are they delivering intra-bank? You know, is it ...

Chief Executive, Jersey Post:

They will have a combination of products, but the products all have to be over £1.30 now. So you are looking at the courier market, which would probably charge, I do not know, £10 or £12 for a delivery as opposed to the mail market. But they also have products, which you have mentioned, which would be patch transfers for banks where the cost of transferring that product will be over the £1.30.

The Deputy of St. Mary:

Okay. So it is in direct competition with the core business?

Chief Executive, Jersey Post:

It is in direct competition with the core business, but it is a pouch of mail as opposed to individual pieces that would have been potentially posted through the postal service, but it is presented as an express product. So the single cost of the pouch is the price that takes it out.

[10:15]

The Deputy of St. Mary:

I was going to ask whether in the context of competition the sacred nature of the mail, the sacrosanctness, you know, the fact that when you put your packet or your letter in the mail it is somehow safe; is that an issue in competition at all, that there is some kind of compliance mechanisms around that, that the others also have to build into their models, or is that something that other people can skate over?

Chief Executive, Jersey Post:

In reality, if you look at the licence conditions of the two other operators locally, there are clauses in those licence conditions similar to what are in ours around the integrity of the mail. How robustly the J.C.R.A. impose those conditions. I do not know, is the answer to that particular question.

The Deputy of St. Mary:

But there are conditions?

Chief Executive, Jersey Post:

There are conditions.

The Deputy of St. Mary:

So presumably there is a cost attached to those conditions?

Chief Executive, Jersey Post:

There should be a cost attached to those conditions.

Chairman, Jersey Post:

Again, in the context of this whole subject there is another consideration, which is Her Majesty's Revenue and Customs requirements for the way in which mails are presented as they go into the U.K. and are available for examination and scrutiny. One of the big issues about the proposal to liberalise the fulfilment market is H.M.R.C.'s (Her Majesty's Revenue and Customs) anxieties and indeed local customs anxieties formally expressed in the consultation with J.C.R.A. that the proposed licensees do not comply with the memorandum of understanding that we are obliged to with the U.K. authorities with - and we will no doubt come to it later - a very significant risk that non-compliance, as far as we are concerned, that there is a very serious risk that the already sensitive issue of V.A.T. (value added tax) payments due on goods going into the U.K. from Jersey will be exacerbated because of the non-compliance with the memorandum of understanding which is a feature of the way the 2 proposed licensees will present. They will present as freight, not as mail. So there is a bit of a loophole there. Our concern is that it will escalate even further their whole issue of the low value of consignment relief in the U.K. and lead to a sanction which will destroy that industry here.

The Deputy of St. Mary:

Right, so we have to keep it tight.

Chairman, Jersey Post:

Well, it is hard to imagine how one can do that because the memorandum of understanding between the U.K. authorities and other postal operators is limited to national postal operators I think probably because of the absolute necessity for compliance. So, it is hard to see how other than a national operator can be given the ... can be seen to comply with that memorandum of understanding. Anything you want to add on that?

Chief Executive, Jersey Post:

I think you are right in terms of the outline. Perhaps just for clarification, the memorandum of understanding, as the Chairman says, is ... you are only able to operate that as a national postal operator, whereas the freight scheme is a bulk import scheme into the U.K. It is a legitimate scheme, but the concern with H.M.R.C. is very much the visibility of their product because the memorandum of understanding, which is a tripartite agreement between ourselves, local customs and H.M.R.C., is very visible. It allows for the collection and pre-payment of V.A.T., the administration of the scheme is with us and it starts ... the compliance starts at the customer's premise and we have compliance people that work for us - we have two now. Whereas the other scheme, there is no local compliance. The compliance starts at the point of this bulk freight going into the U.K., so the visibility disappears right back to the customer because to be part of the M.O.U. (memorandum of understanding) - this is probably the link through to E.D.D. (Economic Development Department) - you have to be an authorised trader if you want to come and set up a fulfilment company to join that M.O.U. To be an authorised trader you have to have a licence to trade from E.D.D., so there is a link right the way through there. The authorised trader scheme does not apply to the bulk exports, and that is where the visibility starts to really disappear, I guess, from H.M.R.C.'s point of view. I think what I would add to Mike as well at the moment I think it is reasonable to say that there is modelling happening in the U.K. to lower the V.A.T. threshold. There are three lots of modelling being undertaken by H.M.R.C. for U.K. Treasury to see what that looks like. Clearly, we have got a new government in the U.K. who are looking at a spending cuts regime and tax reform regime, which is quite important as well. It is quite a big target politically. The sensitivity is around the L.V.C.R. (low value consignment relief) and the Island being used as a "post box".

The Deputy of St. Mary:

I think we are probably going to have to come back to the L.V.C.R. and we will also possibly come back to the M.O.U. and the customs under ... when we talk about specific ... you know, these specific bids that people have got for bits of your market. So is there anything else about the context of where the competitors are coming from?

Deputy M. Tadier:

I think I am happy that has been taken care of. I think essentially the first 2 questions have been

answered.

Chairman, Jersey Post:

I think, if I may, just before we leave that, I just want to address what might be a misconception. We have publically protested at the manner in which it is proposed to open this market to competition. I think we have said it as often as we can, but I am not sure the message is either conveyed or believed. We are not opposed to competition per se at all. We think it is healthy, we are used to it. What we are very concerned about is the execution of the concept, which we regard to be irresponsible and potentially extremely hazardous to the universal service that we are obliged to provide.

The Deputy of St. Mary:

Yes, I think that is probably the next question: what do you see as the consequences of increased competition on your operations?

Chairman, Jersey Post:

I think a healthy consequence is probably intensified pressure to increase the efficiency of Jersey Post's operations. We were already well on the way to taking out 25 per cent of Jersey Post's cost base, which is largely a people business, as you might imagine, between people, Royal Mail ... payments to Royal Mail and shipping between here and our overseas markets. That makes up all of our costs. It is not a capital-intensive business; it is a people-intensive business. So I think probably one of the things that we are dismayed about is that we shared with J.C.R.A. 18 months ago, probably, the detail of our programme, which we were already making good progress with, to take just over 20 per cent of our cost base out through some difficult efficiency improvements. There were job losses involved. You will be aware that back in February, was it, we announced 80 redundancies of posts to disappear. There was some backfill there on lower terms and conditions. Nevertheless, that was part of a programme which would have taken out nearly a quarter of our costs over a 3-year period. We were then somewhat surprised at the apparently arbitrary nature of J.C.R.A.'s decision to liberalise the only profitable part of our activity, which according to J.C.R.A.'s own consultants would require us to take out over £6million a year – which unless we did,

would pitch us into loss making. We will go into perhaps the detail if you consider it relevant later on. But in essence we are now faced with a job-losses programme which represents about 50 per cent of the organisation. We were confident in our programme shared with the J.C.R.A. prior to their announcement of their intention. The one that was taking about 20 per cent of our cost base out over a period of 3 years we considered to have attendant risks which we could manage, risks to users, risks to the capability of the organisation and risks to the shareholder as well in the collapse of the company. It is one of the many issues that we had in our mind to preserve ... to avoid as a risk. The impact of the proposed full liberalisation of that fulfilment sector presents a very different profile of risks to the various stakeholders. So the impact on Jersey Post, I think of the proposed competition, comes more from the pace with which it is being proposed to be implemented and the scale of it. It is virtually unprecedented for a regulator in any previously monopoly market to open that market to competition in one fell swoop. Prudence, caution, whatever, risk management, has always led to staged openings by regulators through various mechanisms, but all have the same effect. Open up a part of the market, make certain the market is stable, and then open up more of it. I think our concern here is ... it arises largely because the J.C.R.A. has always refused, because I think it has not got the resources, to do the Regulatory Impact Assessments, which every other European regulator is obliged to do before it implements a regulatory decision that could have consequences for the sector, the industry, that it applies to. We believe that it is fatally flawed in the way that the execution is proposed. Not the principle, but the execution.

The Deputy of St. Mary:

Yes, I did pick up that thing about the R.I.A. (regulatory impact assessment) and the fact it has not been done here because that seems pretty crucial. Can I just then test your statement when you said that every other regulator - presumably in the E.U. (European Union) - would generate an R.I.A.?

Chairman, Jersey Post:

They are obliged to under European directive.

The Deputy of St. Mary:

Obliged to under European directive?

Chairman, Jersey Post:

Yes, and that is quite specific and we can send you a copy of that directive if it helps.

The Deputy of St. Mary:

Yes, or the number. Because that is a case where we are just not seeming to comply with best practice.

Deputy M. Tadier:

Can I ask if we bring it back to this concept of healthy competition and you said in principle you are not adverse to that. Of course, there is the idea of a level playing field as well, so in the sense that all these other competitors do not have to, first of all, deal with the U.S.O., they are not delivering letters at a loss, so is that a consideration as well?

Chairman, Jersey Post:

It is a fundamental one because the reality is that around the world postal operators have seen the universal service obligation become loss making because of reduced volumes. The whole issue around how one deals with a loss-making universal service provision is one that is taxing the industry as a whole. The ways you deal with it are you change the scope of the service to reflect other technologies, communication and technologies, and we have ... that is central to some of the cost savings that we are making. So that is in terms of in our context reduce the number of deliveries and collections in a week, the number of delivery and collection points, and the retail network in terms of access to sub post offices, for want of a better description. So we are moving rapidly to try to eliminate what is a £5 million a year loss in the combined letters and retail network, essentially the universal service obligation that we have. But it is hard to see that we can never be in a position where that universal service obligation will be profitable. So the notion of a cross-subsidy for that cannot be avoided. So the question is ultimately is it a matter for the public purse and for government to subsidise and that happens in the U.K. and some other jurisdictions, or is there a capability for the operator, the postal operator, who has the burden of that universal service to find other ways from other service offerings to cross-subsidise it. That is at the heart of this issue because

that is what the fulfilment sector provides – it is such a big postal user as a sector that the single figures percentage profit margin we make on the postal service we provide to each fulfilment company provides cumulatively just enough to offset the losses in the USO – but I must emphasise, it's the volume rather than by its excessive pricing.

[10:30]

It is the sheer volume of the fulfilment mailings in Jersey that enable Jersey Post to cross-subsidise the losses on the universal service obligation. It is not an issue that the fulfilment customers are paying excessive prices for that service.

The Deputy of St. Mary:

Well now, there are a couple of questions there, are there not? We will come back to the not paying excessive prices, because that is a key, is it not?

Chairman, Jersey Post:

Yes.

The Deputy of St. Mary:

But the other question is the £5 million the loss you are making on the U.S.O. Somewhere in here there is a claim that ... well, I know exactly where it is; it is High Speed Freight, and they say that the J.C.R.A says that the U.S.O. costs you £100,000 to £150,000.

Chief Executive, Jersey Post:

Yes, and we started that discussion some years ago.

The Deputy of St. Mary:

So how can the J.C.R.A.'s estimate be £100,000 to £150,000 and your estimate be £5 million?

Chief Executive, Jersey Post:

It is not now. The J.C.R.A. have engaged consultants called Frontier Economics who have now agreed that the funding gap is £5 million. That was agreed towards the end of last year.

Chairman, Jersey Post:

They have a report which we have been able to see under confidentiality, but you may well be able to exert your authority. The Frontier Economics report on the impact on Jersey Post of the proposed licensing. It is dated March 2010. It looks very much like that (showed the title page of the report) and it is probably 100 or so pages. That does acknowledge the £5million... and the J.C.R.A. has too, the scale of the losses in providing universal service.

The Deputy of St. Mary:

Right, and they say £5 million?

Chairman, Jersey Post:

Yes, they do.

The Deputy of St. Mary:

That is March 2010?

Chairman, Jersey Post:

Yes.

The Deputy of St. Mary:

Okay, so they just sent that thing in before they had read the other one.

Deputy M. Tadier:

Surrounding the U.S.O. - and I know we are going slightly off the question plan, but that is probably to be welcomed in some ways - that is the core of the issue, both Jersey Post and politically for us, that there only seem to be really 2 or 3 options which would be fair. If we as a government are asking you to carry out a service which is loss making, like the U.S.O., it is only fair that you either

get paid for it directly, so we as a government, which we are not doing now, say: “Okay, we will cover the costs of that. It is a service which is socially beneficial and economically beneficial to the Island” or we give you a privileged position, which you have had up until now, whereby you can cross-subsidise. But it seems that the issue commercially, we are talking about with a free market and with businesses, they are saying: “We are not happy that we are having to pay over the odds for packages to be delivered so that it can cross-subsidise” so that this is really the conundrum that we have to deal with, is it not? What are your views on that?

Chairman, Jersey Post:

I think we share the shareholders’ view as expressed by the Minister for Treasury and Resources it should not be a public subsidy. You know, you will be aware of the fundamental principle of the universal service obligation around the world, that that was a quid pro quo traditionally for the privilege of having a monopoly. Now, as monopolies have been eroded there has exposed the whole issue of how you do fund the U.S.O. in the industry globally. In our case it is ... there are a couple of huge issues here. A regulator would take a view normally, in the normal marketplace, that opening the market to competition, even in the extraordinary circumstances of opening it 100 per cent, that competition would take some time to establish. It would give the incumbent operator time to adapt. What appears to be just not recognised by J.C.R.A. is the whole issue of the concentration of the customer base here in the marketplace in the market segment that they propose to liberalise. So, in the fulfilment market Jersey Post has got - and again these numbers are all in the Frontier Economics’ report I just referred to - which hopefully you will be able to see, or you might well require us to provide you with it knowing that we have got it - we have got 14 significant fulfilment customers as Jersey Post, only 2 of which ... or rather just 2 of which represent 75 per cent of all the revenues. So, an incoming competitor need take only ... one customer which represents nearly 50 per cent and off the record that is (company X. Company Y – names removed, commercially sensitive information) makes up much of the difference. The rest are small operations. So, this is not a case where competitors will have to spend a fair amount of effort and time to go around and win thousands of customers. In the jurisdictions that normally see this kind of liberalisation then you could assume that there would be millions of customers that your new competitors would have to win from you. Here, because of the uniquely concentrated nature of that market, an incumbent

would need to, at best ... sorry, at worst, apply itself to winning 2 customers and at best just one. That cherry picking is such an obvious behaviour that that is for us the principal risk to the postal service provision in Jersey. It arises from the concentrated nature of that very unusual distribution of the market in fulfilment.

Deputy M. Tadier:

When would your contract be up for renewal, if that is the way it works?

Chief Executive, Jersey Post:

Our contract with ...?

Deputy M. Tadier:

Well, do you ever renegotiate your position with the States of Jersey as to what your obligations are periodically, or is it just a rolling thing?

Chairman, Jersey Post:

It is rolling, is it not?

Chief Executive, Jersey Post:

It is a rolling thing.

Chairman, Jersey Post:

In terms of the definition of a U.S.O., yes.

Deputy M. Tadier:

Because it seems that if it were the case we would just sit around a table and say: "Look, if you guys want us to bring in competition ... do you want to bring in competition, then we will compete with that, but we are no longer going to provide a U.S.O. We will not do that." Then that you can provide your own U.S.O.?

Chairman, Jersey Post:

That is exactly it. I mean, that frankly is one of the fundamental absurdities of the way this liberalisation is being executed. If the J.C.R.A. had done what it would be required to if it were operating anywhere else in the developed world, if it had done the risk assessment the top risk, I would suggest, would be that as a rational board of directors of a company with the directors having their legal obligations for the business remaining as a going concern, then they would have had to have anticipated that faced with what is proposed by way of opening up the fulfilment sector and say to the regulator: “We are no longer willing to deliver the universal service obligation and in pursuit of a level playing field with our new competitors we will not be carrying that burden.” The question then is who provides that universal service obligation? It is one that has not been addressed other than that there is a very short clause in the proposed licenses that it is intended to, award to initially 2 licensees, which provides for a compensation fund, a temporary compensation fund, to contribute by which the new entrants would contribute towards the cost of providing the universal service obligation. It is our information that that clause in the licence has not been the subject of any discussion between J.C.R.A. and licensees. It is our belief that J.C.R.A. have got no intention of applying it. It is also our belief that it would not be acceptable to the 2 new licensees. So although it is there we have no confidence at all that it will provide for a stable postal market.

The Deputy of St. Mary:

That is interesting because I picked that out of your submission that you were very sceptical about whether this levy could work or would work and I wanted to ask you what the basis for that scepticism was because you say there pretty well: “Well, it will not work.” Because you have picked up that it is not going to be applied, or is there something else as well?

Chairman, Jersey Post:

One is the behaviour. You know, we do know that it has been completely skipped over in the discussions that have been going on for over a year between J.C.R.A. and the proposed licensees. I think frankly it is a philosophical objection that J.C.R.A. will have in applying it. I think their ideology is for pure market economics. We have not yet seen any pragmatism. So those are 2 issues and the third is there is something rather peculiar about the notion that ... let us ignore for one minute

the economy's ... the savings that we are well on the way now to making in the cost of providing that universal service obligation. So let us just say that we made only modest progress in getting the cost of that service provision down. There is something peculiar about the notion that you open a market up for competition and then you impose a tax on the new service providers to cover the losses in providing a universal service obligation, the net impact on customers will be probably very little different to the status quo. So, we cannot really see how it will work.

The Deputy of St. Mary:

Right, yes. You say here - I am sort of pushing this point because it is pretty important - "There is no tangible evidence to date that this particular approach has been successfully deployed by other regulators." So are you saying that these levies do not exist elsewhere or that they have been applied and nothing comes out of them? So what is the issue?

Chief Executive, Jersey Post:

The concept exists elsewhere in other regulated jurisdictions, but in the work we have undertaken we have not been able to find any hard evidence of the concept being applied or working generally across Europe.

Deputy M. Tadier:

There is a difference, of course, hypothetically speaking now, between all of the operators funding collectively or partly funding collectively a completely separate U.S.O., which would not be administered by Jersey Post in its current form, or 2 or 3 other operators contributing to fund Jersey Post delivering the U.S.O. I think the first one is probably more equitable.

Chairman, Jersey Post:

I think that is right, absolutely. I think we would prefer a situation where it was at our discretion whether we applied to operate that service. A compulsion to do it ... I think, you know, what we would be very reluctant to see happen is that there would be constantly allegations by the new entrants that they were funding inefficiencies at Jersey Post as a tax on their businesses. I think it would be very hard, even in the wake of 50 per cent manpower reductions and all the pain that Jersey

Post is going through to get there, it still would not persuade people that what the new operators would be saying about the residual cost burden was rubbish. But the fact is this is a declining industry in terms of the scope of the universal service obligation and the letters business is a declining business; it is not like telecoms and energy and transport where there is ... the anomalies in the model for liberalising that market are protected in their consequences by increasing revenues. That is not the case here. We are structurally exposed and deficiencies in the model for liberalising this market will not be covered by increasing revenues with the telecoms being a very obvious parallel here that it has been a badly-fudged liberalisation of that market to the extent that you have had duplicate and triplicate investment in infrastructure when it should not have happened at all and that has been borne ... the cost of that has been borne by the lost opportunities for lower costs for users. Here, there will be no hiding from a fudged execution.

Chief Executive, Jersey Post:

I think the other important point just in terms of context to make is both Jersey and Guernsey are quite unique in the structure of our postal operations and unique in the context of the proportion of our overall volume that is bulk export volumes for ourselves and Guernsey Post is no different for the same reasons.

[10:45]

That represents ... over 50 per cent of our total mail volume that we handle is straight off the Island bulk export. Across Europe, U.K., that is roughly about 25 per cent of their total market. If you go to somewhere like the Isle of Man, their export business is 6 per cent. So when you take that in the context of trying to fund an infrastructure for the U.S.O. you have got a very different model. Certainly my experience at the J.C.R.A. is they will pick pieces of regulatory best practice and impose it, but you are trying to impose it on a model that is fundamentally different to the model that that has worked on. That proportionality issue of the market makes it even more of a challenge for somebody like Jersey Post. If we stay with the Isle of Man, the Isle of Man at the moment, only 6 per cent of their total volume is exported off the Island, so the revenue for all of it funds the whole infrastructure; whereas for Jersey Post ... it is nearer to 60 per cent of our total volume disappears

off the Island, so you have got much less revenue staying directly on the Island to fund your fixed-cost infrastructure. So very different models. They are all workable, but they need a different approach and different answers. I think just in clarification as well, I mean, you talked about the scope of the U.S.O. We cannot really negotiate that scope of the U.S.O. 5-day week, 6-day week, whatever it is; it is determined by the licence issued by the J.C.R.A. That licence, the initial guidance from ... it was not E.D.D. at the time, I am trying to think what the name of the committee was, but it was the equivalent of E.D.D. at the time, was for a minimum of a 5-day week, but the J.C.R.A. decided to impose a 6-day week. There is a question mark now over whether government ... well, there is a question mark now whether government can dictate a change to that, or whether it is the regulator that has the final word on what that scope of that U.S.O. will be. So we are not able to renegotiate that. What we are able to do, as Mike says, we are able to say: "We are very sorry, but this is just not a viable business any more; we do not want to apply for the national postal operators' class 11 licence any longer" which is ... the practicalities of that ...

Chairman, Jersey Post:

That is not an abstract concept at all because as you will see when ... I have no doubt you will get the paper on which J.C.R.A. made the decisions from Frontier Economics, Frontier Economics has just 2 scenarios presented as the consequences of the proposed licensing on Jersey Post's finances. I mean, to that extent they have done some risk assessment, but they have not looked beyond the impact on Jersey Post's finances. They should look at the impact on the postal service in Jersey. Two scenarios they give: that is that one scenario, Jersey Post loses one of its 2 largest fulfilment customers, but is able to maintain its profit margins on all the rest of its business. The second scenario is that it loses one of its 2 largest fulfilment customers and is subject to margin pressure as a consequence on all its other business. In that second one, which we regard to be more likely, we cannot imagine that losing our biggest customer would leave us with all the other trading conditions not under pressure, not under pricing pressure. So the only one of the 2 scenarios presented by Frontier Economics to the J.C.R.A., the only one that makes any sense at all, is that we lose either Play.com or ILG and we are under pricing pressure on everything else. In that scenario the numbers here predict - and we agree with them - that Jersey Post would make £7.5 million losses over the first 3 years, which on top of the restructuring costs that we were already underway with - I said to you

we had got a 20 per cent cost reduction programme already underway - makes a little over £9 million in losses over 3 years. Jersey Post would be insolvent in year 3.

The Deputy of St. Mary:

Even with your cash reserves?

Chairman, Jersey Post:

Yes. We started the year with £9.5 million cash reserves. Again, that is in this report by Frontier. The real implication of this is that because of the new Financial Reporting Council's regulations on going concern statements by directors, the directors will have to sit down and my estimate is that in next summer, the next set of accounts, the board, I think - if this liberalisation happens in the way that is expected - then will not be in a position to give a going concern declaration as far as Jersey Post is concerned. That will have pretty profound implications. That is not us scaremongering; it is a fact of life and is a fact of our responsibilities as directors. So, it is just not an abstract notion that we will lose some money, but then we will be able ... you know, we will find a way of overcoming it.

The Deputy of St. Mary:

I lost the detail of when you would be in that position of not being able to give a going concern statement.

Chairman, Jersey Post:

Well, the going concern statement that directors have to make, it was until this year, quite specific, that the directors had to declare that the business was in a position to meet its liabilities for the 12 months ahead. Now common corporate governance standards are that that period is 1-2 years ahead. So, 1-2 years ahead would take us into the beginning of the third year of the liberalisation. That is when it would first bite. It would not be a question of: "Well, all this will come blasting into the public attention in year 3" it will happen probably halfway through year 1.

The Deputy of St. Mary:

That you will start seeing these things?

Chairman, Jersey Post:

That we will have to say that we are not a going concern.

The Deputy of St. Mary:

That there is a risk?

Chairman, Jersey Post:

Well, that is the difficulty. You would say: "Well, okay ..." one of the judgments we would have to take as directors is, is it probable that the £7.5 million losses in the 3-year period predicted by the J.C.R.A. and its consultants, to what extent is it possible that a recovery of mail volumes might help to restore some of our cash flow? As directors we really would have to examine our consciences before taking an optimistic position when in fact the regulatory authorities would probably be punitive in their response if, in fact, we knew it was a risk, it was defined in here, in this report to the J.C.R.A. as a risk, however we decided that we would take a more optimistic view of it.

The Deputy of St. Mary:

Is it just the board's decision, or is it the auditors? My understanding was that the auditors could not sign it off in the auditors' accounts ...

Chairman, Jersey Post:

That is the backstop. The responsibility lies entirely with the directors to make that statement. However, if the auditors believe that the directors were intentionally or unintentionally misleading basically the stakeholders then it could qualify the accounts and, as you say, refuse to sign them off.

The Deputy of St. Mary:

Okay, right

Chairman, Jersey Post:

We have yet to come across auditors quite rightly that would encourage an optimistic rather than a risk-weighted attitude to the declaration of the directors.

The Deputy of St. Mary:

So you have spelt out the consequences of increased competition on the business.

Deputy M. Tadier:

But the thing that is concerning, just to summarise what I think we have been talking about, is that it seems only fair that if competition is going to be brought in and your conditions have changed, your privileged position with the U.S.O. obligations attached to it, that you will be given the opportunity to then renegotiate your side for the U.S.O.?

Chairman, Jersey Post:

Yes. We have already made that application, which we had to make to the J.C.R.A., at the beginning of the year. So we wanted, as a first step towards rationalising the U.S.O., 2 ways of making the cost more bearable, one, as I mentioned earlier on, change the scope of it and the other, fulfil it more efficiently. We are doing both, so we are tackling the cost base with a very substantial job-losses programme, and also finding alternatives to Royal Mail as service provider because that market is now starting to open up in the U.K. and elsewhere with alternative providers for that infrastructure service. But also we said we said we want to reduce the deliveries to 5-days-a-week from 6 that is specified. We got nowhere with that with J.C.R.A.

The Deputy of St. Mary:

Can we tackle the U.S.O.? We will come to that later in more detail. On competition, I just want to look at the cross-subsidy issue and sort of elicit your comment on the sort of things that the ... not really the competitors or the proposed competitors say, but the industry, the fulfilment industry, they say: "Look, you cannot take more from us than you would if you were not running the U.S.O. and then use the extra profit to fund the U.S.O." There is an issue of principle there. I just wondered what your comment on that is.

Chairman, Jersey Post:

Well, Ian will give more detail in a moment, but just to get the understanding of what is at stake here, the largest of the 2 proposed licensees has declared that - and we have also seen evidence of this - they believe they can undercut Jersey Post fulfilment prices by 10 per cent. Now that assumes they have no burden of sharing the cost of the U.S.O. So we are not very far apart in the pricing proposition that we offer to the fulfilment industry locally. It could be argued that part of the social cost of doing business in Jersey where organisations like the fulfilment players are able to exploit, not without risk to Jersey and its reputation and its relationships with the U.K. Government ... there is this exploitation, for want of a better word - and I do not mean it in a derogatory way - of the unique position that Jersey has with respect to V.A.T. in the U.K. Exploiting that should command some social obligation, some contribution, to the benefits that accrue to those shareholders. I think just one thing that strikes me as being a fundamental anomaly here with the whole notion of a liberalisation of this fulfilment sector is that in any competition proposal you find that there are winners and losers. The losers are the incumbent operator. The winners are largely virtually all of their customers. Here, it is rather different to that. The proposed liberalisation has a very small number of winners: the owners of the initially 2 postal operators to be given licenses, certainly 2 of the major fulfilment companies, and maybe some of the remaining 14 or remaining 12 fulfilment companies that are fulfilment companies of any size at all. So you have got less than a handful of beneficiaries from this competitive policy. The losers are the general public and perversely, perhaps, the fulfilment sector employees themselves. But because of the likelihood that the liberalisation will bring the fulfilment industry's prolife up, not just because of what I have spoken about earlier about the way that the memorandum, I am understanding, is going to be undermined by the method of presenting these goods into the U.K., but also that there are other applicants, other postal authorities that have said they either have recently or they intend to soon apply for a license to operate here.

[11:00]

We have met, they have approached us, we have had discussions with these operators and they, quite ignorant of the sensitivity around this whole issue, proudly boast that they believe that they can triple the size of the fulfilment industry in Jersey and: "Would it not be nice, Jersey Post, if we could do

something with you and share in that whole new business opportunity?" They are fairly stunned when we talk of the political sensitivities which would certainly prevent that kind of growth happening, or if it were allowed to happen, because it could not be controlled, it would certainly in our view bring the collapse of our entire fulfilment industry. We sympathise with some of the policy decisions that have been made here to contain the activities of the fulfilment sector in Jersey, because we do believe that what is at stake here is the industry as a whole and a large part, 1,000 people or so, who are employed in that industry probably would not easily find work elsewhere. So I think this is where the ratio of winners to losers that you would normally expect in a competition initiative is completely turned on its head.

Deputy M. Tadier:

Another loser, of course, is the shareholder, I think you may have mentioned that, which is, I believe, our Minister for Treasury and Resources in principal.

The Deputy of St. Mary:

We will come to Ministers and how they relate and the fact that he is sitting there on his own in a minute. You said undercut prices but 10 per cent, I am quite surprised it is such a small difference.

Chairman, Jersey Post:

Well, we are not surprised because we are constantly, as you might imagine, exposed to threats from certainly the largest of the fulfilment customers.

The Deputy of St. Mary:

They will go.

Chairman, Jersey Post:

They are going, they will leave Jersey ...

The Deputy of St. Mary:

Which is my next question, what is the evidence for ...

Chairman, Jersey Post:

So we have spent a lot of time and effort and engaged consultants to keep us very much aware of what the alternative propositions available to the fulfilment sector are and that margin did not surprise us at all. We did not expect it to be bigger because if there are other service providers out there that could offer significant reductions compared with Jersey Post prices, then some of the bigger fulfilment companies would have already gone. Some have gone in the past and come back again and we do know that there is not an offering out there that is very different to that 10 per cent. Ian can elaborate on that.

Chief Executive, Jersey Post:

Yes, because I think at the end of the day whatever competitor does the upstream work it is going to be the same delivery agent in the U.K. which is Royal Mail, because they are the only nationwide door to door delivery service. They may well access it through a downstream access arrangement as opposed to a commercial mail sharing arrangement being put in place. But those are avenues that are open to us and we are talking to Royal Mail Wholesale, the people who have provided us with downstream access, so it is fairly transparent and delivery being a big part of the cost. That piece is quite transparent so we are out there looking and it is no real surprise, as Mike says, that 10 per cent is ... Of course these people want to make a profit as well.

The Deputy of St. Mary:

The 10 per cent figure, where do you derive that from?

Chief Executive, Jersey Post:

That is based on evidence that has come across my desk around what pricing propositions competitors have been pushing through to some of our existing customers.

Chairman, Jersey Post:

It is also stated explicitly in the Frontier Economics paper to J.C.R.A.

Chief Executive, Jersey Post:

It will vary on the type of product but that is the bulk of the product.

Deputy M. Tadier:

How will you be able to compete with that 10 per cent difference? Will you be able to reduce your prices? Are you limited by how much you can?

Chief Executive, Jersey Post:

I think that is back to the circular argument about the cost of the U.S.O. and funding that U.S.O., and that is becoming much more of a challenge now in terms of our profitability over the last two or three years.

Deputy M. Tadier:

Why not just get rid of the U.S.O. if that is the stone around your neck and you are being asked to run a commercial business rather than a public service, just get rid of the U.S.O.?

Chief Executive, Jersey Post:

I think that is the option that ...

Chairman, Jersey Post:

It is one that appears not to have been anticipated by J.C.R.A. as a risk, but you would expect as a rational company that is the first action that we would take.

The Deputy of St. Mary:

Just one question on the costs, it may not be relevant to fulfilment at all but one of the pieces of evidence from Trinity Consultants: "It presently costs us £5.64 to send a kilo of goods to U.K. mainland with Jersey Post and this is before the proposed price increases for sized based pricing. In comparison Citipost will offer the same with service with collection and delivery at £2.15." Now, is this nonsense or is this special selected evidence or what?

Chief Executive, Jersey Post:

I would suggest it is fairly selective, because it depends on what product, which is the point I was going to make before. If you look at the product pricing that we have submitted to you there are categories of product, there are letters, there are large letters, there are packets and the pricing varies greatly across those packets. The challenge you always face and certainly in our experience in working with such a diverse range of product that the fulfilment customers produce, is people tend to go straight for an average price, whereas if 70 per cent of their volume is in this category and only 30 per cent is in that category the average price becomes quite misleading. So I would not suggest anybody has made anything up but I would suggest the calculations are probably different in that example.

The Deputy of St. Mary:

Okay, I just wanted to ... before we go on there is something that has occurred to me as we have been speaking, Mike mentioned a company and said: "Off the record." What do we do about that? Does that come out of the transcript? Does it have square brackets? He also mentioned another company.

Mr. T. Oldham (Scrutiny Officer):

We can certainly deal with that once the transcript goes to you. If you think that it should be extracted, obviously it has been mentioned.

The Deputy of St. Mary:

We have had this in another hearing where people wanted to majorly change things and we just said: "Look, it is what you said" but this can be carried under some other protocol that we can take out specific names and specific companies.

Chairman, Jersey Post:

If that can be done, please do, yes.

The Deputy of St. Mary:

I just thought I needed to check that. The other thing was that the data you prepared for us arrived,

thank you very much. It arrived on Friday, we have not seen it so we will look at that so you can always say: "It is in the data" as you just have. Right, so I think that is everything on the principle of cross-subsidy and on competition. There was one other point which is I have the letter from the Minister for Treasury and Resources and it is not about his relationship to you or relationship to the process, it is about what he says here. He is writing to the J.C.R.A., I do not know if you have seen a copy of this, but what he says is very concerned - this is the end of April - about the issuing of the licenses: "It will have a significant impact on your operations and particularly the company's ability to meet its U.S.O.. As shareholder, I require the company to operate in a financially sustainable manner. The company *inter alia* has to generate sufficient revenue to fund its operations, including its U.S.O. Jersey Post is currently self funding but is dependent on the large letter and packet service as an integral part of the overall business." So this is exactly what we have been talking about. "I am advised the issuing of additional licenses potentially puts the funding of the U.S.O. at serious risk." He says: "I want you to consider these issues." i.e. the J.C.R.A. consider these issues. My question to you is: is there any legal or backstop in terms of the J.C.R.A. having to take any notice of this at all? It says: "Please, I would ask that you consider these issues in your license determination." Is there anything that says the J.C.R.A. have to consider these issues?

Chairman, Jersey Post:

We have had some fairly frank discussions with the Ministers for Treasury and Resources and Economic Development about the potential consequences of this proposed liberalisation. We have discussed with the Ministers the extent to which a direction can be given to the J.C.R.A. which would address the worst of those risks. We are advised that - and it may have changed because this was several months ago - there was not a practical facility which could be used to force the J.C.R.A. into a certain course of action. So meaningful discussions appear to be the only way in which an independent regulator, fiercely independent - not unusual of course for regulators ... that meaningful discussions look to be the only resort. I understand that the Ministers did take legal advice on this and that legal advice was not clear so I am afraid that is all we know, unless you are aware of anything that has happened in the last couple of months?

Chief Executive, Jersey Post:

No, I cannot up date on that one, but the J.C.R.A. have a legal obligation under the Postal Services Law and I am a little out of touch with this one, they used to have two primary duties. One of those the wording is around a sustainable U.S.O. so there is a duty in the law that the J.C.R.A. have to consider those. I think what happens is, that is absolutely fine because then you come back to the circular argument and the economic argument that says: “Well, that is fine if you just take out £5 million worth of cost.” So they probably do give consideration to it but it is how that is interpreted through in terms of the advice, so how can that work, and it is very simple.

The Deputy of St. Mary:

I suppose what I am digging for is, you know, is there some way of ... and you have said basically the Ministers have declined to use their powers under Article 9 of the Postal Law, they have not directed the J.C.R.A. to do anything in particular and there does not appear to be another legal way of dealing with these issues.

Chairman, Jersey Post:

There does not appear to be, no.

Deputy M. Tadier:

But I think too, what I would say the backstop is the political aspect and it does say that the Minister for E.D. (Economic Development) does have to bear in mind the provision of the universal postal service and if we, as States Members, feel that he is doing that we can step in, in the States, and make sure he is fulfilling his obligations, I would suggest.

Chairman, Jersey Post:

Yes.

The Deputy of St. Mary:

I suppose that is ...

Chairman, Jersey Post:

I think so and our biggest concern in this case, as in the general case of the J.C.R.A., is because of their refusal to do regulatory impact assessments and because of what is quite frankly an under resourcing problem in the J.C.R.A., there is a mismatch between the aspirations of the J.C.R.A. board and the capacity of J.C.R.A's officers to fulfil those aspirations in a responsible manner. There is a mismatch, to my mind, between the **authority** the J.C.R.A. has and the **responsibility** (witness emphasis) it feels in discharging that authority. So throughout the piece in our dealings with J.C.R.A. there has been a major concern which is unintended consequences. It is inevitable that regulators are not fully informed on the industries that they regulate. It takes a long time and a lot of dialogue and a great expense of consultants as we have found - because we are having to bear that cost - to get them in a state of competence to understand the impact of their decisions. There have been unintended consequences which you have identified with some of the other licensing decisions Ian spoke about with 2 existing licensees. This is the biggest issue we have got with this, it is sleepwalking into a crisis which is why we have felt that we have had to confront the Ministers for Economic Development and Treasury and Resources with the potential consequences of this action. So we agree entirely the political influence is probably the only resort. We are encouraged, I have to say - and this is not a personality issue - that the new Director of J.C.R.A. has demonstrated full awareness of these risks in the way that he has managed the introduction of competition in the Guernsey market. It is a phased introduction, it recognises the challenge of providing universal service and looks to us to be a measured way of bringing the forces of competition to bear on the incumbent but without the risk of a nuclear incident and, you know, in terms of fallout with provision of the public service.

The Deputy of St. Mary:

Any comment to make on the fact that in Guernsey the Guernsey Post went to court with the regulator?

Chairman, Jersey Post:

I think probably they had very little option because I think they were contemplating ... well, we contemplate in terms of impact and I think they probably felt a duty to challenge what they could see as being a ...

[11:15]

I mean, I have to say I am quite convinced that part of the problem has been in Guernsey that Guernsey Post has not responded - as indeed the electricity incumbent has not responded - to the legitimate pressures that the regulator has been bringing for cost efficiency. I think probably off the record, but we are perfectly happy to substantiate it to you, that regulator - the new J.C.R.A. ...

The Deputy of St. Mary:

It is not going off the record really, unless we go to a private session right at the end.

Chairman, Jersey Post:

Well, we understand from direct conversations that the new Director of J.C.R.A. who is currently in that role in the O.U.R. (Office of Utility Regulation) believes that Jersey Post has anticipated ...

The Deputy of St. Mary:

Some of the issues.

Chairman, Jersey Post:

... properly the very pressures that it should be subject to in a competitive market.

The Deputy of St. Mary:

Right, okay. We are 45 minutes from the end, I am wondering whether we think a little a bit ... I was going to look at the other bits and the actual specifics of the competition because I think that is important and then maybe go on to the ... what do you think, shall we do the Ministers or the U.S.O.?

Deputy M. Tadier:

Well we have dealt with the U.S.O. I think fairly exhaustively.

The Deputy of St. Mary:

A little bit. Yes, okay.

Deputy M. Tadier:

Unless there is anything ...

The Deputy of St. Mary:

Quickly go back to the U.S.O. and then the relationship and then we will try and get back to profitability if we have got time. So the other bids, the Citipost bid for example, because I do not think there is much you have to say specifically on the Hub bid but the Citipost bid you are very critical of it and I just wanted to sort of explore that a bit with you. In your submission to J.C.R.A. of 18th May 2009 you talk about Citipost and in a sense you say that their business model cannot work, if I can quote it to you: "It is about the fact that they are going to take mail unsorted, present it to Royal Mail who are then going to un-bag, sort and re-bag." You cannot essentially see how that can work. In addition, Citipost say: "We are not going to have any people in Jersey at all." So, first of all, is that kind of a fair statement of the position and secondly, just comment on this bid, this proposed licensee?

Chief Executive, Jersey Post:

I think our understanding has moved on a little bit from 2009 but that was the time of the initial notice. I think that the difficulty was all of the sorting activity is undertaken on Island at the moment, so there is a huge amount of resources employed by the fulfilment companies themselves to undertake their sort. When I talk about sort that means what we would refer to in technical terms as a residue sort, so we sort it to 126 postcode destinations in the U.K. and then we hand that over to Royal Mail at its distribution hubs for distribution across the U.K. What Citipost were proposing at the time was to move all that activity out. We did not realise at the time Citipost were proposing to undertake that activity themselves in the U.K. so it was unsorted traffic from here, take all the sorting activity out from the fulfilment customers here in a trailer across to the U.K. and then sort in their own hubs, which I understand is the case now, in terms of Citipost. So they would produce the sort, they would then access through a different access arrangement through Royal Mail. But it was that principle of again, you know, you are coming with a price but if you look at the activity that

fulfilment customers have got around sorting there is a cost to that activity. So if you are going to have an access price, a postage price, and you are going to sort for them then there has to be a flow through of cost into that price because it is not free. I think there are lots of options, I am not particularly clear on that point yet as to whether there is automated options available for sorting, which obviously reduce the cost. I understand that Citipost still do a manual sort in the U.K. that was the principle in that particular piece that we could not comprehend, that you were going to just take that piece of cost, which is a big piece of cost, out of a pricing proposal.

The Deputy of St. Mary:

Yes, I just wonder how the regulator takes on board that kind of information, you know, so you are saying you do not see how it can be done but Citipost say it can be done so ...

Chief Executive, Jersey Post:

I am sure it can be done, it was just the price of the proposal.

The Deputy of St. Mary:

Apart from the H.M.R.C. issues which are separate.

Chairman, Jersey Post:

I think that is another issue, which is specific to Citipost, and it is a reality but the J.C.R.A. would no doubt say: "Well it is speculative." The reality is that Citipost has been up for sale for some years and it has not succeeded in finding a buyer. Our concern is that there is a very obvious incentive for Citipost to engage in predatory pricing, basically uneconomic pricing, to increase its revenues in - as we spoke earlier - one customer could step change its revenues dramatically and increase its valuation quite disproportionately. So there is a heavy driver for the owners of Citipost to acquire at all cost increased revenue, whether it is profitable revenue or not is another matter. The multiples on valuation will be quite dramatic and we believe that the J.C.R.A. is not competent to stop that happening.

The Deputy of St. Mary:

Okay, so it is a risk factor, is it not?

Chairman, Jersey Post:

It is, yes.

The Deputy of St. Mary:

Because then they pull out or they are sold. Right, and there is another question, no plan B. A couple of the submissions refer to that, that because you are entirely dependent on Royal Mail, as I understand it once stuff gets to the U.K. So do you have a comment on that, that there is a problem that when the Royal Mail goes down with a strike, for example, bang they are in stook(?), these people. That is what they are saying to the various consultations, they are saying that because there is no plan B with Jersey Post (Royal Mail) there is an issue.

Chief Executive, Jersey Post:

It is a discussion we have with our major customers in terms of risk management, but I think the principle here is any competitor at the moment, and Citipost included, have to use Royal Mail for the final mail delivery because there is not another delivery infrastructure for the bulk of the product. I think where some of the contingency can exist is when you get into some of the larger product, I guess we would call them parcels, so the larger product that goes out, there are other distribution companies in the U.K. but it is a much smaller demand in terms of the fall to earth. So it is quite manageable to find some resilience and some contingency and I think for us we do work with other partners in the U.K. for particular products. But what tends to happen - and this is from experience at the time of industrial action in Royal Mail - to try and purchase an alternative delivery service is a supplier's market and the price just absolutely doubles and trebles, which becomes a real issue against the model that the fulfilment customers operate, because they are used to postal prices, they are not used to paying parcel, courier, express prices for that product. They have got to list, I think, the change in terms of the offering that fulfilment customers offer to their particular customers and I do not think any of us really ... in terms of the bulk of the product delivered nationwide in the U.K., it is Royal Mail that delivers it so it does not matter whether it is Citipost that are delivering or Jersey Post are delivering it. There is no difference, they do not have any more resilience than we would

offer to consumers for the bulk of the product.

The Deputy of St. Mary:

I am puzzled about this plan B because this particular submission says that if it had not been Jersey Post then they would have had other options, but you are saying there would not have been other options because the final mail would have been done by Jersey Post.

Chief Executive, Jersey Post:

The final mile delivery would be Royal Mail. There are other options but the other options are extremely expensive and at a time when Royal Mail are on strike everybody wants to access those other options so the prices go up and I think if you think about Royal Mail they are set up for 80 million items a day. You will not find another operator, parcel, packet or courier business in the U.K. that could even get near 10 per cent of that and most of their operations are set up for around about their market size so when you suddenly get a surge, certainly based on the volumes that we send out and the average we send out is 1 million a day, which is a big ask for an operator in the U.K. So I think alternatives are there for certain products, yes there are alternatives when Royal Mail goes down but we are able to access those same alternatives. I think the only thing that would probably set us aside to somebody like Citipost as an operator, they already have an established, albeit small scale, distribution operation in the U.K. so they have got a network which they could use to deliver some of the product. But it is nowhere near the scale of the Royal Mail network. So, again, it is a bit of perception here, there is a bit of a sell here.

The Deputy of St. Mary:

Sorry, one last question on competition, if it is just 10 per cent, the difference between what your potential competitors say they are offering and yourselves, and if there was a levy that 10 per cent would come down as well, if the levy was imposed too, why is there all this pressure?

Chairman, Jersey Post:

Ideology, in my view.

The Deputy of St. Mary:

Well indeed the fulfilment companies and the Hub(?) and all these people are saying: “Give us these 2 new operators because then everything will be rosy.” But you are saying 10 per cent and then if you add the levy it is going to be very small percentages for changing provider on the core of your business.

Chief Executive, Jersey Post:

I think a lot of it - from past experience over time - is perception, because consumers on Jersey, certainly some of the larger bulk export operators, have not had a choice because Jersey Post is a monopolist. There is of course the price of that choice. Certainly some of the relationships with the larger customers, larger fulfilment customers, now that they are beginning to understand that we have got a common end delivery agent in the U.K. so it is not just about Jersey Post having a monopoly, it is about the whole supply chain, the most important part of which, for them, is the end to end delivery in the U.K. The perception is starting to change. There is clearly price sensitivity, I mean, that is an absolute fundamental for these customers and, certainly on Mike’s point, the spend of the two biggest customers 10 per cent is quite significant on that aspect because of the volume. That is the difference it makes, so there is a huge amount of price sensitivity. I think what is happening now is there is a realisation almost that for certain types of product, very small volume product, there are alternative distribution networks which we access anyway, they come at a different price and a different cost. That market is completely changing in the U.K. in terms of the emergence of growing volumes of online sales is just driving different distribution products through different companies. But the bulk of the product is still Royal Mail is the end deliverer and there is not another competitor for Royal Mail at this moment in time. The piece that has changed is the upstream collection which sits with the downstream access arrangements.

The Deputy of St. Mary:

We have to understand the drives for the introduction of competition.

Chairman, Jersey Post:

When - and I hope you do - get this report I referred to, the highlight at the bottom there, just by way

of illustrating the expectation of a 10 per cent price advantage.

The Deputy of St. Mary:

Right, so I think moving on to the U.S.O.?

Deputy M. Tadier:

Is there anything to ask on the U.S.O.?

The Deputy of St. Mary:

Is there anything to ask on the U.S.O., well I think the question that is in my mind is it is sort of fixed at the moment at 6 days a week in the network and so on, and it is buried I think in the regulations under the Postal Law? Where does it live? So that when the consultation goes out which has gone out to everybody on the Island about what they want from their U.S.O., and then that goes to the J.C.R.A., but the J.C.R.A. does not decide what the U.S.O. is so who decides?

Chief Executive, Jersey Post:

My understanding is that it is the J.C.R.A., through consultation with the public, who ultimately decide what the U.S.O. is, but there is a mechanism that sits around that, through the PSL 2004 that says it has to meet the demands of users. So you have got a circular piece in operation there that says: on the one hand "Let us go out to consultation, let us find out what the users demand of the U.S.O." When it gets to the point of the result of the consultation though, I think there are some options open to E.D.D. and they are probably better placed to answer those options than me, but in terms of how they then, or government, meets its own responsibility in providing guidance and direction to the J.C.R.A..

Deputy M. Tadier:

To what extent is that pushing on an open door? I mean, nobody is going to say: "Actually I want my mail delivered just 3 times a week rather than 6."

Chief Executive, Jersey Post:

I think that is the other point I wanted to talk about in terms of the scope of the U.S.O.. I think if we just set competition to one side for the moment and bear in mind what I talked about in terms of proportionality of the bulk export market, if you look at what is left, which is more or less the letters market and a few packet deliveries on the Island, the scale of that has reduced so much in terms of volume over the last two or three years, you really have to ask a question about - and I think, Deputy Tadier, you mentioned the social provision - what value are we prepared to put on that? First of all what is the scalability of that, so you have got a postal infrastructure that has absolutely lost most of its economies, principally because there is not a dependency on post that there used to be to do business or to communicate.

[11:30]

Post still exists, we deliver post on a regular basis but the dependency is not there. So there is a piece of work to be done about okay, what is the ultimately sustainable, and what is an efficient U.S.O. on the basis of we are now in a very, very different place with postal services than what we were perhaps three or four years ago, in terms of losing economies of scale. I think once we have decided that, we have got the other piece that says what is an efficient cost and I think that is an important piece because if we go back to the 80 voluntary redundancies we pushed out earlier this year, that was 80 people out of the organisation but we reorganised the jobs based on a skills levels, so we now pay an awful lot less for the labour to undertake those tasks. It is quite important, I think, that we do that because the cost of those or the activities are now more akin to what competitors in the marketplace pay. So there is a piece about what is an efficient cost for that U.S.O. once we have decided what is the right scope for the U.S.O. and I think we cannot step to one side of those two factors because there has been such a shift in the industry. I think your point entirely, you know if you ask the question of people: "Do you want your mail delivered three days a week?" There is a very simple answer to that: "No." If you ask people: "Do you want to keep to 6 days a week deliveries?" There is a simple answer to that: "Yes please, because I have always had it." The reality is ...

The Deputy of St. Mary:

But do you want to pay £50 each?

Chief Executive, Jersey Post:

Other part to the question, absolutely. So somewhere in the middle there, there is a model that will meet consumer expectations but I think when we start to talk about - I think you made the point, Deputy Tadier, about the government funding it - so what price is the social value of that network?

The Deputy of St. Mary:

Yes you have to be careful you get it right.

Chief Executive, Jersey Post:

There is no question about the fact there needs to be a postal network but I think that from many years of experience and if we look across to Europe most of Europe does not deliver on a Saturday now. So that particular model, somewhere in there ... and I think when we talked about 3 day that is almost the stark reality. That is if you just had to build a postal infrastructure based on revenue from letters that you deliver on the Island, you could not afford sensibly more than 3 days a week. That is a simple revenue drop because we have just lost so much of the economy of scale we used to have.

The Deputy of St. Mary:

Is Jersey Post doing a submission to the consultation or have you done a consultation on the U.S.O.? How great does your position sit, or does the J.C.R.A. come to you and say: "This is what the public are telling us, this is our take on it."?

Chief Executive, Jersey Post:

No this is more a public consultation and I would expect us to sit down with the E.D.D. in the first instance and talk about the outputs and then the J.C.R.A., so it should inform a discussion. But I think it is so fundamentally important to recognise competition at the time and there is inefficiency and then there is an inflated social value to something that simply cannot sustain itself anymore because it is fundamentally changed. So it is still there, it still exists, we cannot move away from the politics of it all and the emotion of it and I was alluding to it earlier, you know it is a very emotional

industry, it is not like the telecoms industry or other industries that are not quite so emotional in terms of people's expectation of that industry.

Deputy M. Tadier:

Is it reasonable to say that another consequence, perhaps ironically, if it did go to a 3 day service is that you would lose even more of your letter delivering facilities, you would get other couriers, you would get businesses who would normally put their post through Jersey Post delivering it with one of their staff?

Chief Executive, Jersey Post:

I think that is the other side of the argument, we have talked extensively about the competition and the demand of those customers is a delivery service, it is absolutely fundamental that they get their product delivered because that is their business model. There is some scope, it is not quite as immediate, it is not quite next day, but there is also some recognition and I think that is back to your point, Deputy, if Jersey Post were not to deliver on a Saturday it does not mean we could not make a delivery to you on a Saturday at a cost. It is as simple as that and I think it is ...

The Deputy of St. Mary:

Well you could always build in free delivery for States Member. That is a joke. Anyway, it can be done then.

Chairman, Jersey Post:

I think our nightmare scenario is a realistic one and that is that the scope for us to make more affordable the U.S.O. is, as we said at the beginning, addressing that deficit in the provision of that service. The options are doing it more efficiently, we are well down that road, and reduce the scope of it. We believe that the opportunity to reduce the scope of the U.S.O. is going to be very limited. Your point exactly is people are not going to vote for a reduction in service levels and we saw on the single issue of the Central Market Post Office the picture of how difficult it will be to reduce the access to the point where a vote of the States itself compelled Jersey Post to reconsider its decision not to offer a service, or rather, basically not to renew the lease on the Central Market. So it is a rock

and a hard place for us and so we do not believe we will ever get into the position where the U.S.O. is going to be self-funding, because we do not believe we will be allowed to make the necessary scope reductions when the opportunities to provide that service more efficiently have all been exhausted and we will be exhausting those opportunities fairly quickly, you know, within the next 2 years.

The Deputy of St. Mary:

Right.

Deputy M. Tadier:

I think that leads us quite nicely on to the relationship between the Jersey Post and the States. Can you tell us what the relationship is in the legal sense but also in practice between yourselves and the States of Jersey, via the Minister for Treasury and Resources?

Chairman, Jersey Post:

In theory we are an incorporated entity that is wholly owned by the States of Jersey. We have a memorandum of understanding which I suppose embraces several concepts, one is that our performance will be as a modern postal operator meeting the legitimate needs of customers at the lowest cost possible and providing a normal return to the shareholder. Embedded in that is the principle of no surprises in terms of policy making. The reality is somewhat different to that and to my mind, and I have to say I have expressed this to the Minister for Treasury and Resources as owner's representative, that I believe that Jersey Post is set up to fail, simply because although in theory the incorporation was: "You go off into the big world and you will sink or swim depending on your ability to perform as an efficient operator" the reality is that the level of interference day to day and in terms of our strategic responses to the new threats that we are exposed to ... I mean, it was hand in hand that the very day of Jersey Post's incorporation was the day by design that Jersey Post was exposed to sector specific regulation, so joining Jersey Telecom in that position. So the opportunity was incorporated and, therefore, ostensibly free, commercially free. The threat was: "Well, you are out there now, you sink or swim and you are now exposed to regulation and now we see competition." The reality is we have quite intrusive - scrutiny is probably a too strong a word for

it but in terms of activity the shareholder is far more intrusive in Jersey Post than any other of the many organisations that I sit on the board either as Chairman or as an ordinary non executive director, and these are listed companies so normal institutional shareholders principally, normal shareholder behaviours. But, you know, the Treasury is highly intrusive in terms of the detail in which it wants to get ... we still see it as a States department by Treasury and have protested that brings a burden on our operations that is not acceptable. It also potentially undermines the authority of the board to run the business as it sees fit and the company, as we have seen, is not free to respond to normal pressures in its environment. It is not free of political interference, simply because the quite proper democratic constitution does give any States Member the opportunity to gain access to what otherwise would be commercially sensitive information and to use it as they think fit and we do see the kind of responses that we got to the proposal to close the Central Market Post Office. We have been thrown into the bigger world to sink or swim but we have our hands tied in the way that we can respond. Hopefully, in theory, the Deloitte report into governance arrangements between the States as owner and its utility interests may well improve the situation, particularly around the clarity with which the obligations - which are currently subject to ad hoc political intervention - on the owned entities for delivering social services and for achieving a balance between efficient pricing and delivering dividend returns to the shareholder is still very, very vague and we can only hope that will be much more accurately defined in the future. But, as I said, set up to fail is not something that I would say lightly. It is a pig's ear of model, of freedom to operate but controlled by its shareholder.

Deputy M. Tadier:

There is a contradiction possibly too, I mean, first of all you said there is a tension, if not a contradiction, between your obligation to offer the lowest cost possible with the other obligation to provide a return to the shareholder which other companies do not have that same obligation to provide the lowest cost possible, they have got an obligation to be sustainable and obviously there is a need to be competitive in that sense.

Chairman, Jersey Post:

Yes, absolutely.

Deputy M. Tadier:

But also maybe the relationship with the shareholder specifically, you can go into some detail, I think there is a contradiction there in one sense because the States, via the Minister for Treasury and Resources, on the one hand expects a return, it expects Jersey Post to be profitable. But on the other hand, I guess politically, it is coming under some pressure to provide competition which in itself is going to undermine the profitability of Jersey Post.

Chairman, Jersey Post:

Yes and, I mean, you have seen it obviously in the telecoms sector as well. I think frankly I cannot see a way of avoiding that, I think it is a natural contradiction and I think it is one that is manageable if there is not operational interference with the organisation concerned; us in this case. I have to say the Minister for Treasury and Resources has been outspoken in his determination not to interfere. You know, he has articulated his belief that he should be hands off as an owner, not for him to interfere, but the reality is that our ability to respond to these changing external circumstances will be very much more constrained than if we were simply a 100 per cent State owned but incorporated and, therefore, enjoying the delegated freedoms that our board would expect to have and which we have in theory. I think there is much less scope for us to respond commercially to the threats that are in the market we are operating in, simply because of the politics surrounding our ownership and the unpalatable things that we have to do from time to time to respond to changing circumstances, like significant manpower reductions.

[11:45]

Again, the Minister for Treasury and Resources has not objected to those, we have not been under any pressure from him to constrain our cost cutting efforts. However, I think the body politic is a different animal in that respect and understandably so. The conflict between the impact on the public and the sensitivity of our political leaders to that works against our commercial freedoms to respond in a way that we otherwise would and respond in a way that our competitors are able to.

The Deputy of St. Mary:

I am a bit puzzled by this because, you came to it at the end where you said the Minister has been hands off about the job losses, to take that example, and the body politic is more twitchy about it, although you have gone ahead and there has not been a constraint. But that goes with the territory, you know, you are a public incorporation, you have got a U.S.O. which most companies out there do not have to think about, so inevitably the States will take an interest in what you are doing. When you say you have less scope to respond it seems, from what Ian has been saying, you have been able to do this, you have talked to Royal Mail, you present papers and you keep your independence and you try to drive efficiencies and you run the business. So exactly how does this work out? Okay, the Minister comes and has conversations but you know the States get up in arms occasionally, there is headlines the paper, but you still run the show.

Chairman, Jersey Post:

We do but, for example, the new entrants in the fulfilment sector will feel - and they have already said it is their main objective - able to take whatever commercial action they would in any other market to grow that market. They would encourage new organisations being set up and in fact one of them proposed to set up their own pick and pack operations to increase the size of the market here. They would feel free, until there was specific intervention as has had to happen once before, to engage in the shipping of products that are not available to us because of the political sensitivity. So, for example, certain pharmaceutical products not regarded as being appropriate activity for Jersey Post so we have had shots across the bows: "Do not touch that, do not do this, do not do that." We do have a robust ... and I think it is welcome we have got a robust Minister in his determination to see the commercial model unencumbered, but the reality is that one observes that he himself comes under the pressure of parliamentary questions and the sensitivities ... what happens is we do not get directives: "Thou shall not do this." We get warned of the potential consequences and how much we might be bringing upon ourselves if we do this or we do that. So it is very subtle and possibly it is the proper model that the shareholder, who has a political agenda as well as a normal shareholder's agenda, has meaningful discussions with a sole player. That will change when the control that can be exerted over the postal sector is diluted by competition and just going right back to - sorry, because I drifted off there - your question was: "Well, why is there this issue between freedom to

operate commercially and you would be subject to pressures in any other market, what is wrong with that?" I think that where you have a government that has a set of interests which attract costs to them and expect the incumbent to observe certain protocols, some of them politically driven, you would expect that you would still reserve some sector of the market to fund these off balance sheet activities and off P. and L. (profit and loss) activities. You would not expect a contradiction in saying: "Right, there you go, you are a postal operator with certain social obligations to fulfil but equally we are also subjecting you to the full forces of competition through 100 per cent liberalisation of the only profitable part of the postal service." You would have expected some facility for the government, or the owner, to ration the extent to which you were, as a social service provider, exposed to it. That is my point about the biggest issue here is not the principle of competition, it is 100 per cent opening of the only part of the market that makes any money, that is what is wrong. If you speak to J.C.R.A., J.C.R.A. would say to you no doubt: "We are facing liberalisation in this market. We are going to open up all of the fulfilment sector but it is then afterwards that we will open up the letters market."

The Deputy of St. Mary:

Thanks very much. They are queuing up to take your letters for you.

Chairman, Jersey Post:

Exactly. That is precisely the point and they do not appear to recognise the absurdity of that argument and in fact we would much rather that they opened up the whole market at the same time and ...

Deputy M. Tadier:

Or open up the letters market first perhaps.

Chairman, Jersey Post:

Absolutely. Yes, absolutely. Because that is where the risk to the provision of the social service exists is in that sector and if it cannot work there then why would you take away the only funding mechanism for it, other than the public subsidy.

The Deputy of St. Mary:

Well that brings us on to the Minister for Economic Development then because we talked about the shareholder who comes along and sits in the A.G.M. (Annual General Meeting) on his own, I take it. I have this picture in my mind of the Minister for Treasury and Resources sitting on his own in the A.G.M., is that really what happens?

Chairman, Jersey Post:

No, no, he comes along with Treasury officials.

The Deputy of St. Mary:

With officials, yes. The Minister for Economic Development is the one who has got to handle the J.C.R.A. and is obliged to do certain things under the Postal Law, what is the relationship there, what is the dialogue there?

Chairman, Jersey Post:

There is no formal mechanism there or, indeed, there is no history of a routine dialogue other than when it is issues driven, so fulfilment industry issues. Quite famously a few years ago with the curtailment of that sector's activities which drove 100 redundancies at Jersey Post - we think it was the right thing - it was practically overnight. We think it was probably the right thing because it did address the risk that the fulfilment sector was running out of control and would be so provocative to the U.K. authorities they are closing.

The Deputy of St. Mary:

So that was the Minister for Economic Development at the time doing that to the fulfilment industry, and had there been any discussion with you, did you have any warning of that?

Chairman, Jersey Post:

We had warning of it and to be fair we alerted to some of the risks because there were 2 lots of intelligence sources here at work, one was the U.K. Treasury and between them and Economic

Development - or rather perhaps more at a higher level than that even - and ours was through our role on various European bodies that are represented bodies of the postal industry and their links with government, hearing about the U.K. government's concerns around some of the fulfilment growth offshore.

The Deputy of St. Mary:

I think that is slightly puzzling, you say there is no way of ... it just seems a very limited dialogue and the J.C.R.A. is ...

Chairman, Jersey Post:

It is not habitual, and I suppose you could argue that is how it should be, that the part of the States that has the link to the J.C.R.A. would not feel the need to engage with an operator like us, that they would expect the J.C.R.A. to do that on their behalf. I mean, I do not know if you have got a different perspective on it, Ian, as the Chief Executive?

Chief Executive, Jersey Post:

No, I think it is about the regulator being too close to the regulated and that is the separation that has to exist. I think, as Mike said, there is no formal process to communicate with E.D.D., we do have discussions with them but the challenge, I think, is around what E.D.D. have set up in terms of the J.C.R.A., the powers that the J.C.R.A. have and, I do not know, it almost seems an apparent lack of direct powers that E.D.D. have to direct the J.C.R.A. It is quite a complex little web but that is the way regulatory regime works. I think that is the point I was making earlier about the scope of the U.S.O., it is not within our gift. Yes we can lobby and yes we can talk and we should be doing so, both through Treasury and through other politicians and through the J.C.R.A. to say: "This is what we feel needs to happen." But ultimately the decision seems to rest with the J.C.R.A. in terms of what that scope is going to be. I think the mechanism that will test that is the outcome of the E.D.D. consultation and the scope of it, so at that point when there is a known outcome there is clearly a process to go through which I understand will turn it into a White Paper for government debate first before it gets presented to the J.C.R.A.. It is that point I was making earlier about the presentation to the J.C.R.A., I am not clear whether it could be presented as a direction or whether or not it is

presented as a discussion that says: “We want you, the J.C.R.A., now to reconsider the scope of the U.S.O.”

The Deputy of St. Mary:

My reading of this is that our regulation is prescribed by the States which govern the U.S.O., so that suggests that a change comes to us. It suggests that. Whatever happens before that, the fact on which it goes from 6 to 2 or 3 or 5 a weekend and 5 a fortnight, I would have thought that would come to the States in some form.

Chief Executive, Jersey Post:

I think that is the plan, from the outcome of the consultation. I think the balance is, and it is probably the joined up piece that we will find is quite difficult, if we look at the broader economic arguments, we have to support the fulfilment industries for our economy. Absolutely fundamental and supporting competitive pricing, protecting it in terms of the L.V.C.R., because there is a lot of fragility around L.V.C.R. going forward anyway. On the other hand we have got the postal service, the social service, that we also have to protect. So I guess my comment would be perhaps if there was a different mechanism that pulled the interested parties closer together in terms of the broader, not the just ownership of postal ... and I think that is the difference between a true commercial company and having a government owner and a government representative as a shareholder. So there is a mechanism somewhere there that exists but it is fundamental that the balance is maintained between protecting that industry, which is so important to us, protecting a postal service - whatever that looks like - and a postal service for me that is fit for purpose in the 21st century will still be there, and managing the politics right the way through that.

The Deputy of St. Mary:

That seems a good note to end, it is that time, 12.00 p.m., is it? Yes, is there anything more that you want to say that you feel has not been said, any points that we have not covered? I know we are well aware we have not talked about efficiency at all but I suspect there is a fair bit of data in there and we are aware about the job losses and so on.

Chief Executive, Jersey Post:

Efficiency, if I can just add to that, the J.C.R.A. are just about to complete the efficiency review.

The Deputy of St. Mary:

A second one.

Chairman, Jersey Post:

I think it is that J.C.R.A. is process driven and it just seems to us absurd that because in their timetable of some time ago there was an efficiency review to be done now, they are going ahead with it and it would be completely meaningless because Jersey Post will look nothing like the one they are doing the efficiency review on by the time they are reporting. It is a nonsense and I think the difficulty is it is the cost of such activities by the J.C.R.A. since we incorporated 4 years ago, the regulator has cost us £3.2 million, both in license fees which is a little over £1 million, but more significantly in the consultancies that an organisation like us has to engage because the J.C.R.A. engages with top 5 consultancies.

[12:00]

There is so much at stake for Jersey Post and in our view the service provision, that you are almost in a battle of might and it all costs an awful lot of money. I have just been advised that because J.C.R.A. has overspent on its cost of regulating the postal sector, that our fees are going to go up by 60 per cent. This year some 25 per cent and the year after about a little bit more than that. So we will watch this space because you might imagine against a backdrop of savage cost cutting that we are having to impose throughout the organisation, we are not going to tolerate that kind of cost increase.

Deputy M. Tadier:

Can I just ask, it does bring us back a stage, but you mentioned about the pharmaceutical idea before and that you came under pressure not to pursue that. What was the rationale, first of all, and what was the ...

Chairman, Jersey Post:

I mean, it is one of several influences where there are activities and I do not disagree with it because of the controversy around some unregulated pharmaceutical products supplies into the U.K. from offshore. Then there is the risk, there is a political risk which I think is probably a legitimate one to flag up. From our point of view, there is a commercial risk that if that is one of the things that brings down the whole of the fulfilment sector then we will all be suffering much more rapidly than we otherwise would.

Deputy M. Tadier:

Yes, but it is not necessarily the same form of pressure that another deliverer would ...

Chairman, Jersey Post:

No, and I think this is our biggest concern about the capacity of the J.C.R.A. to properly police the decisions that it makes. I mean, there are 2 issues of which we do not believe it has the capacity to understand the impact of some of its regulatory decisions, but further down stream we do not believe it has the capability to police what it thinks it has imposed on licensees. So by the time the J.C.R.A. would catch up ... I am sure that if you said to the J.C.R.A.: "What do you think your obligations are to prevent such activity?" They would say: "It has got nothing to do with us, that is for the operators to decide." Well that is all well and good but the consequences of intimidating behaviour from that sector would be quite substantial for Jersey Plc, in terms of its relationships with the U.K. government, but also from our point of view - and as we said before - it could bring down the whole of the fulfilment sector.

The Deputy of St. Mary:

All these questions are so intense because it is a small Island, everything has a magnified impact.

Chairman, Jersey Post:

Yes, it is disproportionate.

Deputy M. Tadier:

Well what form did that pressure come in? Was it just a conversation in the corridor or was there a board meeting that suggested that?

Chairman, Jersey Post:

Part of the requirement of our M.O.U. with the Treasury for sharing business plans, sharing strategy, we spoke about some of the options open to us to mitigate the profit impact of liberalisation and we spoke about: “Well, you know, we have some significant opportunities, for example, to ship for Guernsey companies.” A lot of Guernsey fulfilment companies want to have Jersey Post as its provider, for all sorts of commercial reasons, and we were warned there and then: “Well, that is something you cannot touch (specific products).” There have been others and, you know, frankly because we see the sensitivity around them we needed to understand the risk attitude, given the new circumstances. I mean we might have expected - I am not saying we did - the shareholder to say: “Well I see that our dividends are at a huge risk here, I want you to take whatever commercial action you feel is legitimate. As long as it is within law, you do it.” Well it is not that way, it is much more refined.

Deputy M. Tadier:

Because normally a shareholder would not have to face question time as a politician does.

Chairman, Jersey Post:

Yes, exactly, and I think that is the dynamic that does make the difference here, because I think you have probably observed and I have said Philip Ozouf is robust in so far as he - protect is the wrong word, but he is a stage between the questions of some lobbyists and the compunction that Jersey Post has to answer any questions no matter how sensitive they might be commercially. The Minister is an effective filter to take some of the rubbish of that out. What happens when it is a different Minister, maybe one less robust? That is when the model I think of an incorporated but 100 per cent owned entity like us will be severely stretched.

The Deputy of St. Mary:

Is it fair to say that you see the solution in the government's arrangement, that you touched on the big report, that is that thick, about the governance of the utilities and that if it was specified what your role was more precisely in there and what the trade off between dividends and social obligations was, and the obligations for the workforce as well which we have not mentioned, then it would all be in there and then we could say: "Okay, we will do it."

Chairman, Jersey Post:

That is it, but I do not believe that will ever happen. Because of the democratic process I cannot see that Jersey Post will ever be sufficiently detached from political sensitivities to be able to fulfil some of its obligations through commercial freedom. At the moment it has not been a major constraint on us. There are several areas where our activities have become controversial, Ship2me the route to be able to facilitate internet shopping. We were not prevented from pushing that ahead, however, we were constantly aware of the sensitivities around it and anticipated a lot of them.

Deputy M. Tadier:

Yes, in a memo I think as well certain States Members have raised this idea that one States department, well not a department but you know what I mean, is in competition with another States owned ...

Chairman, Jersey Post:

Yes, exactly.

The Deputy of St. Mary:

Welcome to the goldfish bowl.

Chairman, Jersey Post:

Well that is precisely it, so it is inevitable that there are going to be these conflicting priorities and they will shift from probably one quarter to the next, depending on the flavour of the moment and whatever else. But I do not say that disparagingly but there does need to be some rigor around how well it is defined and I think Jersey is not alone in facing that difficult. A recent - it was not that

recent, it was probably 3 years ago - review in Guernsey of the effectiveness of the incorporation processes, it came back that the single biggest failure was the failure to define the precise requirements of the shareholder for the incorporated entity's performance.

The Deputy of St. Mary:

Just leave it to a sort of mish-mash of debate and questions.

Chairman, Jersey Post:

Yes.

The Deputy of St. Mary:

Okay, thank you very much for giving us your time and sorry we have run over a bit but it was most forthcoming and I think that has helped us well.

Chairman, Jersey Post:

Thank you. Would you mind if I retrieved that single page?

The Deputy of St. Mary:

You can have it, absolutely.

Chairman, Jersey Post:

But I will certainly provide the title of it. I mean, as I say, that is the title of it but you might want to refer to it. If you struggle with co-operation from the J.C.R.A. and instead require us to provide it, we will be happy to do that but there might be some expletives in the margin to overlook.

[12:09]