

# STATES OF JERSEY

## Economic Affairs Scrutiny Panel Jersey Post and Competition Sub-Panel

**FRIDAY, 24th SEPTEMBER 2010**

**Panel:**

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

Deputy M. Tadier of St. Brelade

**Witnesses:**

Executive Director, Jersey Competition Regulatory Authority

Paul Hamilton, Jersey Competition Regulatory Authority

**Also Present:**

Mr. D. Scott (Scrutiny Officer)

[10:00]

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

Right, it is 10.00 a.m. So welcome to Jersey. Sunny Jersey. For the tape the first thing we will do is introduce ourselves so that the transcribers know who we are and so on and then we can go on to the hearing. My name is Deputy Wimberley and I am chairing this panel in the absence of the person who is really the Chairman, which is Shona Pitman.

**Deputy M. Tadier of St. Brelade:**

I am Deputy Tadier from St. Brelade and I am just a member of this panel. I have been drafted on from a different panel.

**Executive Director, J.C.R.A.:**

I am the Executive Director of the J.C.R.A. (Jersey Competition Regulatory Authority).

**Postal Case Officer, J.C.R.A.:**

I am a postal case officer at the J.C.R.A.

**The Deputy of St. Mary:**

Our Scrutiny Officer, Darren Scott. Rebecca is taking the notes. Right, as I say, welcome and the terms of reference are fairly broad. We want to look at how J.C.R.A. and the various Ministers, how their operations produce the right answer for Jersey and whether that seems right from that point of view. I understand obviously there are sensitivities around the details of specific applications or specific licences and we will just have to see how that goes in your statement and so on as we proceed. But I did think it was useful, certainly for the tape and for the public if you would say right at the outset how the handover has happened, where you are now as the Executive Director, what is the run in and so on.

**Deputy M. Tadier:**

Can I just interject? We do need to draw your attention to this. It is just basically a statement to say that during the meeting what you say is covered by privilege on the condition that everything that you tell us is to the best of your knowledge true.

**Executive Director, J.C.R.A.:**

Thank you for that. Yes, in terms of my role and position, officially as of 22nd September, as of Wednesday, I am the Executive Director of the J.C.R.A. Chuck Webb, who is my predecessor, and myself have been having a bit of a handover over the past 6 or 8 weeks or so since my appointment was announced. I am reasonably familiar with some of the issues that the office, the J.C.R.A., have been looking at anyway purely because of my role as the Director General of the O.U.R. (Office of Utilities Regulation) in Guernsey. Particularly on the regulated sectors and the telecom and postal sectors, a number of the issues that we have looked at previously in Guernsey have been looked at here in Jersey and certainly in some cases, particularly on the telecom side, we have been doing more and more joint projects anyway. So I have a ... I am not starting from scratch in terms of my knowledge of some of the issues that are being faced. In terms of the handover, basically I will be working as the Executive Director of the J.C.R.A. reporting to the J.C.R.A. board as well as carrying on the role of Director General of the O.U.R. in Guernsey.

**The Deputy of St. Mary:**

Okay, so I think now maybe if you make your statement.

**Executive Director, J.C.R.A.:**

Thank you. First of all can I thank you for the invitation to meet with you this morning. I think everyone has agreed that these are changing times for the postal market and postal customers expectations of what they want and need from the postal service is changing. The demands of, in particular, business and bulk mail is becoming more and more price conscious and the changes in technology, particularly in the telecoms market has meant that the postal service faces very real and very fast changing competition in the wider communications market. This coupled with the current economic climate has meant the need to look at how postal services are provided, what we as postal customers are willing to pay for those services and how a change in the postal market might be managed are all live issues. International developments also have an impact on what happens in Jersey. Currently, as you are aware, the J.C.R.A. is considering applications for postal licences from Citipost and Hub and, as I think we have already informed yourselves, while we are restricted in what we can say on those specific applications I believe it would be helpful to set out at a high level the factors driving the need to look at how postal services are provided more generally. Before I talk about the drivers for competition in the postal market let me talk a little bit more about the scale of change that is occurring in the postal market. I know Jersey Post has already shared with you its views on the historical decline in the postal service and its views on what the future might look like in terms of volumes. I suppose it is worth noting that that challenge and that decline is not unique to Jersey. The Guernsey postal market is under exactly the same pressures and recently the Hooper report, the updated Hooper report in the U.K. (United Kingdom), noted that it expected worldwide letter volumes to fall between 25-40 per cent over the next 5 years. This is fundamental change on a scale not seen in the postal service before. The Hooper report noted that the decline in letter volumes is predominantly structural, caused by things like email and mobile data substitution. So it is unlikely that that decline is going to be reversed. Therefore in that kind of environment the case for maintaining the status quo becomes very hard to sustain. That is

why in the J.C.R.A.'s view, regardless from the pressure from postal customers for choice, regardless of whether competition is introduced or not, the need to fundamentally alter the cost base in Jersey Post is a very live issue. But not only is there a need for change from Jersey Post in such an environment, postal users also need to adapt their thinking and expectations of what is the future postal service looks like, because ultimately it is postal users changing how we interact with the postal service that is causing and accelerating the challenge for the Jersey Post. Let me just give you one example. Last year in Guernsey the O.U.R., the postal regulator, consulted on introducing competition in the postal market there. As you are probably aware, there was some fairly strong criticism of those proposals, not dissimilar to some of what has happened here. But the Save Guernsey Post campaign was predominantly run through Facebook and most of the submissions that we received to the consultation were submitted by email. Now, while the support that people were trying to give to the post office was very well intentioned and very well meaning, I think it just illustrated the fact that as customers we just use communication services, the wider communication services, much differently than we have in the past. I suppose the traditional postal service is not now, I suppose, our first port of call when we look at how we convey messages and information to people. A further example locally, and I do not know if Jersey Post touched on this with yourselves when they met with you, is local businesses using mailing houses in the U.K. to send their things like bills and statements to local customers. Technology facilitates that very, very easily. So again that competition exists in the postal market whether we like it or not. The difference, I suppose, with that type of competition is that it is less visible. There is not a container of mail at the ferry service going out with somebody else's name on it beyond Jersey Post. So those type of challenges exist and they create very real challenges for Jersey Post. So in that type of environment the need for Jersey Post to look at its cost base is critically important. That need exists regardless of whether competition was being contemplated or whether it is introduced, that need is there and it is probably been long overdue. So, as I say, from an ordinary postal customer's point of view we need to perhaps think more freshly about how it is we want the postal service to look in the future. That becomes even more of an issue when we look at the bulk mail sector. The bulk mail sector is a very important part of Jersey's economy, it introduces a level of diversification to the economy that perhaps would not be there otherwise. As I understand it there is about 1,200 people employed in the fulfilment

industry, and those companies purchased goods and services from other businesses. So their impact beyond just the employment and the direct taxes that they pay goes much more widely and deeper into the Jersey economy. But those types of customers compete in global markets. They compete with the competitive services through the internet predominantly, they face competition from other online business. Take for example Play.com, they face competition from Amazon particularly, from HMV in Guernsey, from bulk mailers in Switzerland, Hong Kong, the U.S. (United States), and they also face fairly stiff competition from the likes of the U.K. supermarkets. So all of those issues create a pressure for those businesses to make sure that they can provide their services as competitively as possible. I guess the issue for us in terms of a regulator, as customers and as an important group of customers, they say to us that at the moment Jersey Post is not as competitive on price as they need it to be to support their business. So I suppose the impact of that is that the drive to introduce competition has not necessarily been driven by the J.C.R.A., it is not driven by some kind of ideology on our part. It is very much driven by consumers actually wanting choice and saying for their businesses they need that choice. I think also if one looks at, for example, the likes of Swiss Post, they have come to the Island here and similarly in Guernsey on a fairly regular basis now to talk to bulk mailers to see what can they do for them either here or in Switzerland. So the consequence of that is that it puts real pressure on Jersey Post to get its cost base appropriate. It also puts real pressure on it to make sure that the ... what I can describe as the fat in the charges that it has been charging bulk mail customers is no longer available to it. So it, I suppose, exposes what has probably been an issue for the company - not just here but from postal companies everywhere - which is the growth in the online business has masked to an extent the higher cost base and some of the more outdated work practices that have existed. I suppose if one thinks back to how charging here, similarly in Guernsey, has evolved over the past 10-15 years, up until the late 1990s, early 2000s, Jersey Post, Guernsey Post and Royal Mail had a very convenient relationship for themselves in the sense that they did not necessarily reflect proper commercial charges for the services that they provided to each other. So there was, in effect, an indirect subsidy from Royal Mail to Jersey Post. As that changed, as Royal Mail introduced more commercial pricing, the growth in the bulk mail business has taken off, in a large part due to the growth in broadband penetration on the internet. As a consequence, while the charges from Royal Mail were going up, the growth in volume

from both mailers helped to mask some of the underlying structural issues that exist within the post office. That is not unique to here. Every postal operator has been in pretty much the same boat until recently. I suppose we are really now only at this stage having to properly look at what it costs to provide what I might describe as the traditional postal service. I know a lot has been made about the potential impact should competition be introduced into particularly the bulk mail market in Jersey and the impact on Jersey Post. I am not quite as gloomy about their prospects in a competitive market as perhaps some are. Jersey Post has a quite a number of what I would describe as quite strong cards in its hand when it comes to competing in the market. It has longstanding relationships with these customers, it has the Memorandum of Understanding with Revenue and Customs which gives it some considerable advantage when it comes to quality of service over potential competitors and I know from the situation in Guernsey where very similar arguments were made prior to us finalising our decision that Guernsey Post now itself, I think, would accept that the prospect of competition is not as bad as perhaps they may have initially felt was going to be the case. They recognise that they have challenges in terms of its cost base but it also has some considerable strengths which it is able to bring to the table when it sits down to negotiate with bulk mailers.

[10:15]

I suppose the final point I would like to make just in terms of my opening remarks, is that there is a perception that the only people who benefit from the potential of competition coming into the mail market will be a small number of very large customers. I do not think I would necessarily share that view. If one looks at what Jersey Post is doing at the moment it is tackling its cost base across the entirety of its business. One could say that it is a review that is overdue but the fact is by doing that, all of us who use the postal service, should result in getting a more efficiently provided, a more cost-effective postal service. So I think while there is very direct benefits potentially for some competitors, there are indirect benefits and wider benefits for all postal customers. I think, to be fair to Jersey Post in terms of the work we have done, in terms of talking with them about the changes they are looking to introduce, I think we would say there is a lot to commend on what they are doing. It is a change in the

postal sector. Anyone who has looked at the problems Royal Mail has had will know that introducing change in the postal sector is very difficult and I think from that point of view the way Jersey Post is going about it is ... I think they need to be commended and I think they need to be supported on it because I think we all - ourselves as the regulator, the States as a shareholder, postal customers big and small - need and want a very strong Jersey Post. It is in all our interests that the work that it is currently doing to prepare itself for that, it needs to be supported. I think if it is okay with yourselves I will stop there and, as I say, to the extent that I can I will answer as many questions as you have. If there are very specific issues on some of the licensing applications I may have to defer on those but I would like to have as open a conversation as we can.

**Deputy M. Tadier:**

Thanks for that. It is useful to start off like that. It probably saves a few questions. Can I just ask one about something you said there? I think I just need a further explanation. You talked about the fat in the bulk mail for Jersey Post is no longer there, what do you mean by that?

**Executive Director, J.C.R.A.:**

I think if you look at the structure of charging in the postal service, you have got what I would describe as the 2 parts of the postal business. You have got the services to the fulfilment industry which is generally less labour intensive than the traditional postal services, and what one tends to see is that the charging there perhaps does not always reflect the true cost of providing that service. That is what I mean in terms of there being some fat in the system. That is, in a monopoly market, you see it in the telecom sector, you see it in the electricity sector, you see it in most utilities sectors where there is a monopoly in place, the need to focus on the true cost of providing the service tends to be less than in markets where they face competition. Certainly I know from just looking at Guernsey Post where we have gone through that discussion and we look at the tariffs that it is now looking to ... that it is currently asking us to consider. It accepts that its charging to bulk mailers perhaps has not been as reflective of the actual cost of providing that service. I do not want to leave the impression that Jersey Post is taking advantage of its customers. I am not saying it to be critical, I am saying it merely to make the

observation that I think that we are at a situation now, possibly for the first time in a very long time, of really needing to understand what does it cost to collect and deliver the traditional mail. It is has not been an issue that has been overly important until now because of the previous relationship with Royal Mail, because of the growth in the fulfilment industry since. As I say, it is has helped to mask a number of issues in terms of both work practices and also in terms of cost within the postal service.

**The Deputy of St. Mary:**

You mentioned a couple of times the cost base of Jersey Post and the picture we get from Jersey Post is that they have worked very hard to reduce that cost base, under pressure from the J.C.R.A. as well as just knowing that they have to do that. There is a risk if you go too fast at your cost base that there is an incredibility and the taking of staff and so on. So I was just interested in the different versions we are getting, we are getting from yourself that really they are too slow on tackling their cost base. Certainly in the Guernsey summary in our Green Paper here, the summary of the situation in Guernsey does seem that the situation there is a lot slower in the sense of cutting costs. Jersey Post, I think, would say: "Well, we are quite a lean machine." What I want you to comment on is their assertion that if the customers were so unhappy they would have gone to Switzerland already.

**Executive Director, J.C.R.A.:**

Let me distinguish between I suppose where we are currently with Jersey Post and perhaps where we have been to date. I think in terms of the work that it is currently doing to tackle its cost base ... you know, as I say, I think there is a lot to commend in it. It is looking to introduce what for the postal service, which has traditionally been a fairly slow moving animal, is quite an impressive change. So I do not want to discount what they are doing. I guess the point I would make on it is the type of changes that it is looking to make now or the type of practices that it is looking to address have been in the system for quite some time. These are not new problems. I suppose one would say that the decline, while it has certainly accelerated in the last 2 years has always been there in the knowledge that this was going to happen. So I suppose if one was to be in some ways critical one would say that these were problems that could have been tackled and perhaps should have been tackled earlier.



**The Deputy of St. Mary:**

A question we ask in the States quite often. [Laughter]

**Executive Director, J.C.R.A.:**

Exactly. I accept fully in terms of the challenge that it faces and certainly we are very conscious of the challenge it faces in making sure that it brings its people with it. I think we would be sitting here having a very different postal panel scrutiny committee if Jersey Post made wholesale changes and suddenly the postal service breaks down and we have got ... so we are very, very alive to that issue. It is one of these things where with the postal service, I think distinct from all other utilities, the consumers, postal users, have a stronger emotional attachment to it than most other utilities. In fact, to be frank, to any other utility. That creates ... in some ways that is great because there is almost a loyalty to the business that I think most other utilities would sell their granny to have. But the problem with that is when you are looking to bring about change as a commercial business the pace at which you might to do it versus the pace at which perhaps your customers are prepared for is very different. That is why, I think ... I know the Hooper report has picked up on the fact that Jersey is looking at the whole issue of the U.S.O. (Universal Service Obligation) because it is a critical part. If I go back to one of the comments I made earlier, all of the issues that Jersey Post are facing actually are driven by its own customers because of the fact that they are changing how they use it, what they want from it, the frequency of it, the quality of it, the price of it. All of those issues are changing. I suppose we as customers have to then, I suppose, play our part in helping them make that change. It is a very different mindset, it is a very different approach.

**The Deputy of St. Mary:**

Can I press you a little bit on the question why have the customers not gone to Switzerland? Jersey Post's answer would be: "We have tackled our cost base and we are not that far more expensive that we could be if we really, really went to the cost base. So there is nothing in it really for people to go because there is a relationship there is not with Switzerland, Switzerland is politically dodgy because it

is outside, it is different, the L.V.C.R. (Low Value Consignment Relief) might not sustain it.” So why have they not moved?

**Executive Director, J.C.R.A.:**

I think for individual companies there will be different answers to that question. I do not think there is a single answer.

**The Deputy of St. Mary:**

Yes, it is a bit unfair to ask you.

**Executive Director, J.C.R.A.:**

I think in terms of price the point I would make on it is that up until recently the fact that the mail market in the U.K. is only now really starting to take off in terms of real alternatives to Royal Mail, the likes of Citipost, U.K. Mail, TNT in the U.K. are starting to get their operations now to a level where for part of the supply chain they can really offer an alternative. That is really only in the last 2-3 years that that has come about. As a consequence the prices that Jersey Post have been charging - and I can say the same in Guernsey - have been okay. They know they have been paying a bit more than perhaps they should do but relative to the alternative competitive offerings it was not bad. That is changing. I think for individual companies, particularly those that have quite large volumes, the pressure on price is becoming much more, I suppose, driven, partly by the economic climate and partly by the continuing growth in competition. It is creating that challenge and I think it is making it more of a live issue now. If I can just give one further comment on that, and just referencing back to Guernsey if I may, about 2-3 years ago our office was asked by our Commerce and Employment Department to look at the whole issue of the degree to which the L.V.C.R., its importance in supporting the bulk mail sector because it was quite a live political issue at that time in the U.K. - it was interesting talking to the bulk mailers, and we meet with them very regularly - that up until that discussion really started they were aware that there was alternative channels through the likes of Switzerland, even for Guernsey customers coming to Jersey or looking at alternative markets. Some of them did start to seriously look at it. Seriously cost it

out, seriously look at it. I think the difficulty is that in those commercial businesses at some point the numbers stack up and I guess that is the concern we would have in terms of the J.C.R.A. is making sure that Jersey, as a location for this, is very competitive. Whether that is through Jersey Post, which as I say I still feel they have some quite strong cards in their hand, or whether it is through possible alternatives, I think from a Jersey economy point of view that is still important.

**The Deputy of St. Mary:**

Can I just go back to the L.V.C.R.? What was the genius of thinking about that yourselves, for J.C.R.A.?

**Executive Director, J.C.R.A.:**

It was discussions between the U.K. Treasury, I think, with the politicians in Guernsey and I think a similar conversation was happening with politicians here.

**The Deputy of St. Mary:**

So you just heard?

**Executive Director, J.C.R.A.:**

Yes. Yes. Our office was asked to do some work for the department to support them in terms of their assessment of the issues.

**Postal Case Officer, J.C.R.A.:**

Can I just jump in and elaborate on a couple of things as to why a lot of the Jersey based companies have not moved to Switzerland. We spoke with all the main fulfilment companies in Jersey and while we are aware that, for example, Tesco has gone because it was forced to as a result of its 2006 fulfilment policy, the reason why most of them will not go is because of the cost of relocating. They are tied into long leases with their warehouses, they are generally Jersey based families, Jersey based directors, they see themselves as being based in Jersey and not uprooting all their families and all their history to

somewhere like Switzerland.

[10:30]

That was a point that was coming across loud and clear, which you can sympathise with. The other point is some of the larger fulfilment companies over here employ in excess of 300 people each, so that means making some very, very difficult decisions in laying off those people and then you have got to recruit in Switzerland and train in Switzerland. It is a very, very costly exercise and it is something that they would probably do only in the very last resort.

**Deputy M. Tadier:**

It is fair to say that a lot of the staff taken on by the fulfilment industry are either on probably zero hour contracts or casual labour which is not necessarily going to be possible in Switzerland as well.

**Postal Case Officer, J.C.R.A.:**

That is true, there is going to be a higher ... yes. But what we have been told is the benefits of moving to Switzerland, if they were to do that, is not so much in price because the price ... while Jersey Post is a bit more expensive than Switzerland across the range, the most important thing where Jersey Post is not able to deliver compared to Swiss Post is on quality of service. Where the e-retail market is happening at the moment is in Europe. Jersey Post can get their goods into Europe, minimum 5 days but we have had some reports it takes as long as 10 days. For most e-retailers who want the latest D.V.D. (digital versatile disc) they want it right now. They are not willing to wait for 8-10 days. Whereas if you are based in Switzerland you can get that product delivered across Europe within about 2, maybe 3 days at the very maximum. That is a very, very important consideration, and something that the new licence applicants have tried to address.

**Deputy M. Tadier:**

But that is a problem presumably for any Jersey based deliverer not necessarily just Jersey Post, it is for

any competitor that would come into Jersey that the problem of location is also pertinent.

**Postal Case Officer, J.C.R.A.:**

It depends on what line haul. Jersey Post's line haul all goes up through north and they give it to Royal Mail or mail handlers and then they despatch it across Europe and across the world. We have been told there are other ways of doing that in a more efficient way. For example, taking it south into France and injecting into La Poste.

**Deputy M. Tadier:**

I just have one quick question. I think you have put a very good case for competition coming into the market but what I would ask, and if you can comment on it, I would suggest that it does not necessarily follow that just because the market has changed particularly in the traditional postal service, for example emails, Facebook, et cetera, that necessarily means that it is an argument for competition. You could argue certainly from a political point of view that, because the cost of delivering the tradition mail per letter is going to go up that is even more of an argument for protecting the U.S.O. and the cross-subsidy. What do you say to that?

**Executive Director, J.C.R.A.:**

I would say that in terms of that change in technology I would agree that it is not an argument for introducing competition. It is the argument for why the cost base needs to change. There are, I suppose, separate customers who have very different needs from those who perhaps might use things like email or Facebook and stuff like that. Their needs, certainly in terms of the case they are making to us on this, is that ... let me put it slightly differently. What they are saying to us is that they need more competitive pricing and they are not seeing it from Jersey Post. They are aware from their contacts, as they should, that there are options available to them that are more competitive. That is really, I suppose, if you like, in terms of ... the 2 drivers that you have in terms of the changes in the postal market are driving the need to look at the 2 separate parts of the postal market in 2 very different ways.

**Deputy M. Tadier:**

Yes, I understand, and it is all going to come back to the U.S.O.

**The Deputy of St. Mary:**

Which is what I was going to ask next. I have got a written question answer here in the States, 20th April, where the Minister for E.D. (Economic Development) wrote: “The J.C.R.A.’s assessment of these considerations must include potential impact of the grant of additional postal licences on J.P.’s (Jersey Post) continuing ability to operate on a sustainable basis, including the provision of an U.S.O.” “Must include potential impact of the grant of additional postal licences on Jersey Post’s continuing ability ...” Please comment on this aspect of ... because you mentioned that we all need and want a strong Jersey Post. Their argument is that by opening the profit bit, if you like, to competition their ability to live with the U.S.O. is compromised.

**Executive Director, J.C.R.A.:**

Let me take it perhaps in 2 stages, if I may. The first point I would make is that in terms of our work, in terms of looking at the whole issue of the introduction of competition, we have spent quite a bit of time looking at the implications for Jersey Post in terms of where it currently is and where we believe it should be in terms of its costs. Picking up on something that the Hooper report also picked up on, which is the real threat to U.S.O.s tend to come from the inefficient cost base of the U.S.O. provider. Tackling that is the critical part of ensuring that the U.S.O. is sustainable. That is where we spent quite a bit of time over the past several months looking at the work that Jersey Post is looking to do on its own efficiency proposals. The second part of it is we have spent a fair bit of time working with a very respected economic firm, Frontier Economics, looking at the issues that the potential for competition might have for Jersey Post and the nature of the challenges that it would face in that type of environment. Our assessment of that and our conclusion of that is that with it making the type of efficiency savings that it is currently making - in fact, correct me if I am wrong on this, Paul, my understanding is that they are exceeding their own efficiency plans ... their plans will exceed the type of savings that Frontier had modelled - should put it in a very strong position to continue to be able to

provide the U.S.O.

**Deputy M. Tadier:**

Can I ask in what sense the U.S.O. is not efficient, because from a customer point of view you could argue they are paying 45p, around that price, but a letter to be delivered ... to get service 6 days a week and have it delivered to your door within a day, that seems to be very efficient from the customer's point of view?

**Executive Director, J.C.R.A.:**

In terms of the actual scope of the U.S.O., Guernsey Post interestingly did some work back in about April, it surveyed its customers to understand how important 6 days a week - because the U.S.O. in Guernsey is similarly 6 days a week - is to customers. If my recollection of this is correct, and if it is not I will try and find you the exact figures, it was about 60 per cent of customers said: "We do not need 6 day a week services" and I think if you look at how we as customers are changing what we want from the postal service, if you think about the types of mail that perhaps is time critical, very little of it is time sensitive any more. The stuff that is, things like credit card statements, a lot of people are now moving to the situation where they get that online. Whether you get the credit card statement on the Monday of a week or the Thursday of a week I think to most people is not overly critical. They like the certainty to know they get it ... if their expectation is they get it in the third week of the month or the fourth week of the month, still getting it in the third or fourth week that matters but which specific day I think matters less and less. I think certainly things like the take up of home broadband means that more and more people can use email at home, so for communication with family and friends, needing to have what you could describe as that social aspect of the mail is changing and changing quite a bit.

**Postal Case Officer, J.C.R.A.:**

Particularly when you look at the profile of the mail and the source of all mail, almost 90 per cent of all mail is now generated business to business.

**Deputy M. Tadier:**

But is it fair to say, and obviously I take what you say about the U.S.O. could possibly be made more efficient, that the U.S.O. could never be made to cover its costs. It is a public service and it can never be break-even, let alone be profitable.

**Executive Director, J.C.R.A.:**

I do not necessarily accept that. Certainly if I can talk just in the context of the work we have been doing in Guernsey in looking at the type of pricing that Guernsey Post charges. Not dissimilar to here. A large cross-subsidy from the bulk mail sector to the traditional service has existed. We have been working through successive price controls with Guernsey Post to remove that. Where we are getting to now is, and I think where we are at, a situation where both mailers make a contribution for the general overheads that support its business but they do not, if you like, pay an additional levy to fund the core traditional postal service. That is why I say in terms of ... because in a potentially competitive market the ability to have that kind of extra there diminishes. One needs to make sure that the traditional postal service can wash its own face. Long term that becomes extremely important in terms of sustainability.

**The Deputy of St. Mary:**

Can I ask about the cost of the U.S.O. because it is a bit startling when Jersey Post report that according to High Speed Freight, according to the J.C.R.A., the U.S.O. costs £100-150,000 per year and then now the estimate is £5 million which has basically been agreed by Frontier and Jersey Post itself. That is a huge gap in an estimate of what the U.S.O. costs and therefore the subsidy and so on and all the other issues. So how can you explain the gap, just the process of that?

**Executive Director, J.C.R.A.:**

I think timing. The scale of decline in the traditional mail market has accelerated quite a bit since the first assessments of this were made. I think I can quote - and correct me if I am wrong - our current assessment of the numbers which show probably around about £3 million.



**Postal Case Officer, J.C.R.A.:**

About 3, yes.

**The Deputy of St. Mary:**

About £3 million. So the £5 million has changed again.

**Executive Director, J.C.R.A.:**

The £5 million I do not think was Frontier, originally it was JP's but the work that Jersey Post is currently doing on efficiencies leads us to believe that the cost of the USO is less than £5m.

**Postal Case Officer, J.C.R.A.:**

That is right, it is all about getting the costs down. When we first undertook the work we estimated it was about £150,000. Jersey Post, as you know, strongly disagreed with that. But when we reworked the figures using different methodologies, because postal economists will say there is more than one way to calculate the cost of the U.S.O., we were then seeing huge, huge declines in the market and Jersey Post naturally could not save the costs at the same rate at which we were seeing declining revenues. So on that basis we said: "Okay, it is now more than the £150,000 that we first estimated but we now estimate it is somewhere around about £3 million."

**The Deputy of St. Mary:**

So some detail on it. The £150,000 estimate was when?

**Postal Case Officer, J.C.R.A.:**

That was back in early 2008.

**The Deputy of St. Mary:**

Early 2008 and at the end of 2009 Frontier Economics did a patch of work for you and said it was £5 million?

**Postal Case Officer, J.C.R.A.:**

Yes.

**The Deputy of St. Mary:**

Now you are saying £3 million.

**Postal Case Officer, J.C.R.A.:**

Yes, the reason is, as John has just explained, that Jersey Post is now stripping out costs and so these are forecast figures to the end of this year. It is what we estimate it to be.

**The Deputy of St. Mary:**

Okay. I just want to read you a bit from the annual report of 2007 of Jersey Post because it bothers me; it really bothers me.

[10:45]

“We have until recently been extremely concerned by the absence of any obligation upon the J.C.R.A. [you can comment on that whether it is in the law or not] to conduct regulatory impact assessments before imposing any new regulatory action. Regulatory authorities in virtually every modern economy are required to apply analytical effort proportionate to the likely effects of any proposed regulatory action in accordance with the recommendations of the Mandelkern Group on Better Regulation. Done early and earnestly, stakeholder consultation can form a valuable part of such impact assessment and may in some cases obviate the need for J.C.R.A.’s investment in impact analyses on ...” But the key thing is the obligation. First of all is it in the law? Secondly, what have you done in that area and is it a valid criticism that everybody else can do it and we do not?

**Executive Director, J.C.R.A.:**

My understanding in terms of the law - and Paul can correct me if I am wrong - is that specifically the need to carry out a regulatory impact assessment is not mentioned in the law. Regulatory impact assessments more widely get regulators and particularly incumbents excited like probably no other issue in regulation, which does not reflect well on either regulators or incumbents. Regulatory impact assessments is a very general term that is given to how regulators go about assessing the impacts, the costs, the benefits of a particular measure that they are looking to introduce. The European Union, certainly for European regulators - and certainly I have to say I am more familiar across the telecom sector because of work I did back in 2000 when I was in Dublin on this - have a requirement that regulatory impact assessments are carried out. The difficulty is trying to find 2 regulators or 2 incumbents who will tell you what a regulatory impact assessment looks like because it varies from issue to issue. I know certainly the Better Regulation Executive in the U.K. in its guidance has been fairly clear that there is no one way of doing a regulatory impact assessment. There is also the issue - and this is certainly something that we are very conscious of being a small regulator - of the nature of the resources that either ourselves or Jersey Post would have to do the type of regulatory impact assessments that happen at an E.U. (European Union) level.

**Deputy M. Tadier:**

Can I ask more simply then, I understand that we may not know what an R.I.A. (regulatory impact assessment) looks like but have you done one? Do you feel that you have?

**Executive Director, J.C.R.A.:**

Yes. The Frontier work, as far as we are concerned, was our regulatory impact assessment. If I look at the various different initiatives we take as a regulator, across all of the sectors, the nature of the impact assessment is going to vary. For example, if one looks at something in the telecoms market, you have got a number of competitors in the market, they are able to give us a whole range of views of what they think the impact is going to be. That is very valuable information from the coalface which we can take on board and take account of. In the postal market we are in a situation where we have got Jersey Post, we have got their customers, particularly the bulk mail customers, and we have got potential new

entrants who can all feed into the information that we then sit down and distil and try and come to a view on what is in the long term best interests of Jersey, of Jersey postal customers and indeed Jersey Post. So to give a short answer to your question, yes, we have done what we would consider an assessment of the issues for the postal market here.

**Postal Case Officer, J.C.R.A.:**

Can I just elaborate on that? Under the Postal Law, specifically under Article 8, where our duties are set out, and our duties under Article 8(1) is to ensure that demanded postal services are provided and under Article 8(2) is the secondary duties which are all about promotion of competition, where it is considered appropriate in postal users best interests and in broad terms the economic interests of the Island. The Frontier work that John mentioned, what we did is we undertook some very, very detailed scenario analysis where we said: “Right, if competitors come into the bulk mail market under various options, how will this affect the financial viability of Jersey Post?” We looked at that with our primary duty hat on, i.e. to support the U.S.O. either under a 6 day a week or 5 day a week basis. The results of that showed that J.P. does have sufficient financial resources to sustain competition, even under a worst case scenario and, yes, we did forecast that there would be modest losses in a worst case scenario but it had more than enough cash available to sustain those modest losses. The final point I would make is that we shared all this information with Jersey Post, they actually commended the piece of work that was undertaken by ourselves and Frontier and thought that it was a very, very good piece of analysis. So we are a bit surprised that they are calling for a more detailed R.I.A. type assessment to be undertaken.

**The Deputy of St. Mary:**

Two questions that come out of that. One is ... and the other is ... **[Laughter]**

**Deputy M. Tadier:**

If I can just step in, maybe that will help. One of the consequences that seems apparent to me, and I think Jersey Post have probably already raised this, is they will say that once competition is introduced they are no longer competing in a fair and level playing field in the sense that they have got this U.S.O.

that they have to deliver which the other competitors do not have to, and it is quite possible that either that U.S.O. will have to be renegotiated or they may even consider whether they now, as a business rather than simply as a public service as it used to be, can afford to deliver that U.S.O. We could be in a scenario where they go back to the Government and say: “We no longer want to do this, we cannot do it” and that would have to be funded directly through direct or indirect taxation.

**The Deputy of St. Mary:**

Adding to that what they told us was that within 2 years, and this is why I asked the question about R.I.A.s and I am surprised that they are saying ... they may be saying it is a good piece of work but they may also be saying they do not agree with it because what they told us was: “Actually in 2 years’ time our accountants will not be able to sign off on our thing because we will not be a going concern basis.” Now that is pretty startling that Jersey Post will not be a going concern within 2 years because of regulatory action.

**Executive Director, J.C.R.A.:**

Yes. I suppose the first point I want to say is I have yet to meet an incumbent who was happy with a regulatory impact assessment that produced an answer that they did not like. It really does not matter how much analysis you do if at the end of the day it is a decision that they still prefer is not made they will say there is a need for more assessment. As I said in my opening comments, I do not accept the predictions of doom coming from Jersey Post with regard to the potential impact on itself from competition. I think it is doing, as I said, fairly commendable work itself in terms of tackling its cost base. I still think that competitor wise it is in a very strong position with regard to the bulk mail market. It has quite longstanding relationships with these customers, the quality of service it provides to them at the moment is certainly I do not think a cause of concern. I think some of the bulk mailers would prefer if there was a bit more differentiation in the service, some kind of value adds in the service but I would suggest there is nothing that stops Jersey Post being able to respond to those types of demands in the same way that potential competitors are able to try and service those demands. So what I have read, their comments with regard to that figure and to the potential consequences, I struggle to accept.

**The Deputy of St. Mary:**

Can I move on to a different area? What do you take into account when issuing licences? I have looked at the law. The law seems to say J.C.R.A. can issue licences. So what do you have to take into account in terms of factors that might be worrying when you are issuing a licence?

**Executive Director, J.C.R.A.:**

If Paul can talk a little bit about it, given that he was more involved in the specifics of the initial notices.

**Postal Case Officer, J.C.R.A.:**

Okay. So far to date we have issued, in addition to the Jersey Post licence, 2 others. That is one to Regency Logistics and the other one to High Speed Freight Services. In each of those cases our duties are laid down in Article 8 of the law which I previously alluded to. We look at very simple things: are these guys able to provide better, cheaper, faster, more reliable, et cetera, postal services than Jersey Post? Is the consumer going to be better off? That is basically it.

**The Deputy of St. Mary:**

Can I test that a little bit then? I will just throw one issue at you out of the 4 I have got here: integrity. How do you make sure that the integrity of the mail is preserved with a new licensee?

**Postal Case Officer, J.C.R.A.:**

In each of those cases what we do is we look at their postal operations that they have got in place, we ensure that they have got procedures and operations set up to ensure that the integrity of the mail is well secured. We visit them and we require them to prove to us that those procedures are in place.

**The Deputy of St. Mary:**

Is that part of the licence then? Do you write that into the licence?

**Postal Case Officer, J.C.R.A.:**

That is part of the licence condition, yes.

**The Deputy of St. Mary:**

What would happen if they broke it? If you went along and did another visit and you found they were not following procedures at all or whatever.

**Postal Case Officer, J.C.R.A.:**

We would basically ensure that they would take appropriate measures to address those measures.

**Executive Director, J.C.R.A.:**

Without having the Jersey Post licence in front of me, I expect a similar condition is in their licence. In the same way that if there was a breach of the licence from Jersey Post we would require steps to be taken to rectify that and ultimately, and again this is without the benefit of having the law in front of me, I am assuming there are other sanctions that can be brought to bear. The issue with regards to the integrity of the mail, these are commercial companies, they know that if they get it wrong with something like that it hurts. What we find, certainly if one looks at the telecoms market, is that those commercial incentives tend to be a hell of a lot better at focusing the mind and providing a good service at the required quality than anything that we put in a licence. It has real consequences and very immediate consequences. So I think while the ... it is right that we are alive to the issue and alive to the potential risk, I think we need to however be sure we keep it in the right perspective in terms of how real it is.

**The Deputy of St. Mary:**

Okay, a more difficult one, the compliance with H.M.R.C. (Her Majesty's Revenue and Customs) and the fact that if you send stuff that is over £18 you might need to do a V.A.T. (Value Added Tax) declaration first so they can collect it in advance. Jersey Post handles all that, how can you ensure that the new companies play ball under the same conditions and do not raise the flag that what Jersey is

doing is an issue?

**Executive Director, J.C.R.A.:**

I would say from my perspective there are 2 answers to that. First of all I know from our own discussions with for example Citipost, because they are interested in the Guernsey market and I know from our conversations with them in that market, that they have spent a lot of time talking to Customs because there is issues for them with regard to quality of service if they do not have the Customs side of things correct. Again, I come back to the commercial issue. That commercial issue is very important for those types of businesses. We know that they have spent a lot of time sitting down talking to Customs to make sure that they have got a system that Customs is happy with in terms of processing.

**Postal Case Officer, J.C.R.A.:**

The same applies to Hub as well.

[11:00]

**Executive Director, J.C.R.A.:**

Yes. The second issue, I suppose, is the companies that are here who are asking for choice are all very alive to what I might describe as the political issues associated with L.V.C.R. It is not in their interest to try and have this market explode to a level that raises it as a political issue any more than it currently is. There is nothing in it for an existing customer, for an existing bulk mailer in Jersey who is in a position to comply with the L.V.C.R. and commercially use it to their advantage legally to risk having that damaged. Again, it is entirely right that it is an issue we are alive to, again I just think it is one of these things that needs to be put in perspective in terms of how real the risk might be.

**Deputy M. Tadier:**

We are aware of time. Can I just ask one more question?



**The Deputy of St. Mary:**

Yes, fine. I have got one more factor and then we will deal with your one. The levy. Now that is clearly not something where just running a good business drives you to having taken it to the mail and is something that would protect the U.S.O. and I gather from this document, the Green Paper, the consultation paper, that in Guernsey you consulted about whether the new entrants should be forced to pay a levy to support the U.S.O., and that was an option. Can you comment on that?

**Executive Director, J.C.R.A.:**

The whole issue of funding U.S.O.s, and this runs across the telecom sector as well, is one of these issues where certainly in Guernsey in the telecoms market when we introduced competition all of the licences granted to new entrants contain a condition that if there is what we call an unfair burden associated with providing the U.S.O. that they may be required to contribute to support that. We are proposing similar licence conditions for potential operators, competitors to Guernsey Post, in the postal market in Guernsey. Again Paul can correct me if I am wrong in this, but my understanding is that we are also proposing similar conditions in the postal licences in Guernsey should they be granted.

**The Deputy of St. Mary:**

In Jersey.

**Executive Director, J.C.R.A.:**

Sorry, in Jersey.

**The Deputy of St. Mary:**

Could you go into that a little bit, please?

**Postal Case Officer, J.C.R.A.:**

Sure. The compensation funds, certainly in the postal sector, are all about compensating the U.S.O. of a U.S.O. provider who is providing that service efficiently. So as long as the regulator is assured that the

U.S.O. is right down to efficient costs and the U.S.O. is still deemed to be an unfair financial burden after an efficient operator is providing that service, then regulators will look at implementing a compensation fund. In Europe there have not been ... it is very early days in this area but there have not been any successful examples of compensation funds being introduced anywhere in Europe.

**Deputy M. Tadier:**

Is that because there has not been an efficient U.S.O.?

**Postal Case Officer, J.C.R.A.:**

No, there are 2 examples that I can give. One is in Finland and the Finnish regulator set the compensation levy at 20 per cent of taxable turnover base. Now if you are a competitor with Finnish Post coming in and you have got to all of a sudden hand over 20 per cent of your turnover and give it to the incumbent that is not very attractive. So it is no surprise that there has been no competition in the Finnish post market.

**The Deputy of St. Mary:**

You mentioned implementing a compensation fund, does that mean that there is a condition on the 2 licensees or potential licensees to have a levy but the implementation is a separate stage?

**Executive Director, J.C.R.A.:**

Yes.

**Postal Case Officer, J.C.R.A.:**

The implementation is a separate stage, yes.

**The Deputy of St. Mary:**

That depends on this “must be efficient”?

**Postal Case Officer, J.C.R.A.:**

They must be ... there are 2 criteria, the regulator must be completely content that they are efficient in providing the U.S.O. and after that hurdle has been achieved then they must come and prove that the USO is an unfair financial burden.

**Deputy M. Tadier:**

But you could have a paradoxical situation where if the competition has already been introduced it makes the efficiency of the U.S.O. harder to achieve than if there had not been competition.

**The Deputy of St. Mary:**

Yes, because you have lost the volume.

**Deputy M. Tadier:**

So it is almost a catch-22 situation.

**Executive Director, J.C.R.A.:**

Except, I think, most of the studies, particularly at a European level where they have been looking at abolishing reserved areas altogether, have all come to the view that competition helps with U.S.O.s because it drives that efficiency. If we look in the context of Jersey Post, its original timeframe for implementing savings was, I think, 3 years. The prospect of competition means that can be done in 18 months. I guess that is the distinction I would make between having a situation where you wait until you are satisfied that the operator is fully efficient because in that case its incentives to get on with it are possibly skewed. Whereas setting ... we have been looking at the whole issue of licensing for around about 2 years now. That has been a relatively long lead time in the context of a licensing decision, so the opportunity has been there for Jersey Post to think about what, as a business, it needs its operations to look like going forward. As I say, in terms of ... a lot of what it is doing, we are impressed with it. It is, as I said, a difficult business to change just because it has not been exposed to the type of change that

has happened in the telecoms market and the type of pace at which things have happened in the telecoms market. The postal sector has been sheltered to a large degree.

**The Deputy of St. Mary:**

Although they have already had a savings package in 2006-2007.

**Executive Director, J.C.R.A.:**

Yes, I think if I could, without being entirely familiar with what Jersey Post did, compare it to Guernsey Post, it similarly did some things in 2006 on the back of a previous price control we put in place, yet when we came back to look at in 2009 a lot of things had slipped back in. It is one of these things with compensation funds where we want to be very clear to new entrants coming into the market that one of the rules and one of the conditions of coming in is that in the event that there is this unfair burden on the postal operator you may have to pay. It is pay or play. If you are not happy with that then ...

**The Deputy of St. Mary:**

But the problem is that the new entrant and the incumbent are different people so the new entrant will put political pressure on to say: "They do not need 5 days a week, never mind 6, 3 days will do, why should we pay for 5 days? What about 2 days?" So the pressure is always the businesses telling you: "Why should we fund the U.S.O. at that level?"

**Executive Director, J.C.R.A.:**

Which is why in the context of determining what it is that the U.S.O. should be it is only right and proper, in my personal view, that that is a States view. That we get the guidance from the States on that. With U.S.O.s, and this applies everywhere, there are conflicts with it in the sense of what it is, certain individual groups of users place certain value on different parts of the postal service. For some having access to a post office close by is important, for some having a post box relatively close to the

end of where they live is important. For others getting the post 5 or 6 days a week is important. They might not all at the same time - in fact I doubt if they all at the same time - put equal importance on each one of those components of the U.S.O. That is why in the context of the current review that is ongoing here and in terms of any change should there be a change, it is important that proper weight is given to those various competing components.

**The Deputy of St. Mary:**

So are you saying that as a result of the consultation, and the report is writing by E.D. not yourselves, then that would come with your comments presumably to the States to set the U.S.O. and balancing the demands of the sector so that it is going to be: “Well, the jobs need to be safeguarded but on the other hand we need 3 days a week” or whatever it is, and the States holds the ring in that they will say what will happened.

**Executive Director, J.C.R.A.:**

I think that is purely as a consequence of the way the law is drafted. In Guernsey it is drafted slightly different in that the States can direct us on the ... sorry, it directs us to make sure that the company provides the U.S.O., if I can describe it that way.

**The Deputy of St. Mary:**

Yes, okay.

**Deputy M. Tadier:**

I think we have got other questions, possibly what we will do is if we can email some to you.

**Executive Director, J.C.R.A.:**

Yes, or if you need to me to return I am more than happy to do that. But it is whatever is convenient for yourselves.

**The Deputy of St. Mary:**

Thank you very much. I think one point that did come out was the Frontier report, is it going to be possible for us to have that because it seems to be that is the R.I.A. effectively?

**Executive Director, J.C.R.A.:**

Off hand I am not aware of a reason why we cannot but if you can leave that with me I will certainly come back to you.

**The Deputy of St. Mary:**

If there is confidentiality issues then we can sign things.

**Executive Director, J.C.R.A.:**

There certainly will be confidentiality issues with it because there is a lot of commercially sensitive information for Jersey Post. I think redacting it probably dilutes the benefit of it but if you are happy for me to take that away and come back to Darren I am more than happy to do that. Off hand I cannot think of a reason why we cannot provide it to you on a confidential basis.

**The Deputy of St. Mary:**

Okay. I think that last sentence of yours was quite ... going back to the balancing act, was quite a good wrap up but is there anything you want to say before we say goodbye.

**Executive Director, J.C.R.A.:**

No, but to thank you again for the opportunity.

**The Deputy of St. Mary:**

Thank you for coming in.

**Executive Director, J.C.R.A.:**

Thank you.

[11:11]