

## **CWU submission to the Economic Affairs Scrutiny Sub-Panel – Jersey Post and competition review**

1. The Communication Workers' Union (CWU) represents 215,000 employees in the postal, telecommunications and financial services industries. We are the recognised union for postal grades in Jersey Post and have 276 members in the business.
2. The CWU welcomes the Economic Affairs Scrutiny Sub-Panel's decision to review the Jersey Competition and Regulatory Authority's (JCRA) moves to grant two new licences in the bulk mail market in Jersey and our submission is informed by the responses we made to the JCRA's consultations on these proposals in 2009 and 2010 respectively.
3. However, we are concerned that the Scrutiny Sub-Panel's review was instigated more than a year after the JCRA published its first consultation on the application for a postal licence from Citipost and almost five months after the regulator published its initial decisions to grant licences to both Citipost and Hub-Europe, which were originally intended to become effective on 30<sup>th</sup> April 2010. The decisions are already having a significant impact upon the postal service, employees in the industry, the universal service and businesses in Jersey, and it is regrettable that scrutiny is taking place at such a late stage.
4. As we made clear in our submissions to the JCRA, the CWU is strongly opposed to the proposals to introduce competition in the bulk mail market in Jersey. We believe that the JCRA's decisions to grant two new bulk mail licences will jeopardise the future of both Jersey Post and the universal service and that it is contrary to the interests of the public and businesses on the Island.
5. Together with the harmful effects the proposals will have for postal services in Jersey, against a backdrop of existing international competition in the bulk mail market and the constraints upon growth in the Island's fulfilment industry, we do not believe that the JCRA's proposals will deliver the economic benefits or improvements in service which it suggests will arise. These arguments are set out below.
6. In its consultation the Economic Affairs Scrutiny Sub-Panel is seeking views on the following issues in particular:

- the effects of increased competition on the viability of Jersey Post, private postal/fulfilment operators, employees and the public;
- the roles of the JCRA, Minister for Economic Development and Minister for Treasury and Resources, respectively;
- the performance and efficiency of Jersey Post; and
- the suitability of the Postal Services (Jersey) Law 2004 and Competition (Jersey) Law 2005.

These points are dealt with in turn.

### **The impact of competition**

7. It is clear that the JCRA's proposals to introduce competition into the bulk mail market will have a significant impact on the viability of Jersey Post. In 2009 Jersey Post reported an operating profit before tax of just under £930,000, a fall of almost 80 per cent from over £4.3m in 2008 and £4.5m in 2007. The business attributes this to a 4% reported decline in overall mail volumes in 2009 (with a 13% fall in letters, partially offset by a 5.4% increase in the bulk mail and packet volumes); a £3m increase in Royal Mail's charges to Jersey Post over a two year period (the majority of which has been absorbed in the business's costs); and increasing competition driving down margins (particularly in parcels and the bulk mail market).<sup>[1]</sup>
8. Without a detailed breakdown of the business's costs and income it is difficult to forecast its performance in the future relative to these results. There has been investment in the business – with £1.6m invested in Jersey Post International Development in 2009 – and the company estimates that the move to size-based pricing – introduced in May 2010 – will increase revenue for the business by around £275,000 (approximately 0.4% of revenue in 2009).
9. However, the CWU understands that Jersey Post is projecting that, even without the introduction of competition in Jersey, it will be pushed into a loss-making position in the coming years on the back of a forecasted decline in mail volumes.<sup>[2]</sup> In response to the predicted trend in traditional mail volumes the CWU is working with Jersey Post on delivering significant savings to help sustain the business including a voluntary redundancy programme for 86 employees and the introduction of a new, lower salaried grade.
10. It is clear that, over and above the forecasted decline in mails, the introduction of competition into the bulk mail market will have a significant detrimental impact upon the business. The fulfilment industry represents 60% of its revenue and in 2008 it estimated that the introduction of competition in this market in Jersey would reduce its profits by around 50% - between £2m-£3m at that time.<sup>[3]</sup> A comparable impact in 2009 would have resulted in an operating loss in

excess of £1m for the year – a position which would be unsustainable going forward.

11. In light of these figures, with the business's projected fall in current profit levels from volume decline, the JCRA's proposals demonstrably put the solvency of the business at risk in a short period of time. Indeed, the CWU understand that the JCRA's proposals are based on Jersey Post being able to double the projected cost reductions it is making to sustain the business – which already exceed the targets set by the JCRA in 2007 – and that it has not taken account of increased costs Jersey Post faces as a result of recent actuarial valuations of the pension fund.
12. In our submission to the JCRA we stated that the introduction of competition would jeopardise the universal service and that, in order for the company to survive, the inevitable consequence of the regulator's decisions would be a significant decline in the postal service for the vast majority of users. This would mirror the trend seen in the UK since the introduction of competition.<sup>[4]</sup>
13. Jersey Post has stated that it makes a loss of around £5m on the universal service, which it currently sustains through revenue from its bulk mail business, and it is clear that many of its costs for this service are relatively fixed; lower mail volumes are not reflected by lower overheads, where the same number of deliveries or collections are required to be made irrespective of the number of items being carried.
14. In line with this trend Jersey Post had approached the JCRA to discuss altering the universal service obligation in its licence – to providing five deliveries a week rather than six, to match the minimum requirements of the Postal Services Law (2004) – even before the publication of its initial decisions to grant licences to Citipost and Hub-Europe. In June 2010 the Minister for Economic Development went far beyond this, issuing a Green Paper on the universal service obligation (USO) proposing to cut the USO to as few as five delivery and collection days in a fortnight.
15. The CWU believes that this demonstrates the trade off which is being made between introducing competition in the bulk mail market on the one hand, and maintaining an adequate universal postal service on the other, and we do not accept the assertion in the Green Paper that the impact of the JCRA's proposals on the USO would only be to 'accelerate what would already happen.'<sup>[5]</sup> While Jersey Post is operating within a challenging environment with traditional mail volumes currently declining, it is hard to understand how the introduction of competition into its most important market – taking away millions of pounds worth of revenue, which it is far from inevitable that it would otherwise lose to international competitors – would not independently damage the company and its ability to sustain a loss-making service.

16. The CWU is strongly opposed to the proposed cuts to the USO and we do not believe that such reductions in the core service would be contemplated if competition was not introduced in the Island's bulk mail market. We believe that the USO plays a vital economic and social role and provides a highly valued public service and the union's petition against the proposed cuts was signed by over 3,000 members of the public in August 2010, demonstrating the strength of opposition to the plans.
17. The Green Paper contemplates charging businesses for a daily service which clearly leaves them at a material disadvantage. We believe that this change in postal services would have damaging consequences for Jersey, given that a significant proportion of businesses are smaller enterprises, which are less likely to be able to meet the additional costs being proposed, and on the ground that the largest sectors for jobs – finance and retail – have historically been heavier users of mail.<sup>[6]</sup>
18. A further aspect of the economic impact the cuts to the USO would have, is the increased pressure this would place on our members' jobs in Jersey Post – one of the largest employers on the Island – at a time of high and rising unemployment. Our members have received no increase to basic pay since 2008 and in light of the challenges the business faces we have agreed a voluntary redundancy programme for over a fifth of staff on 2008 levels, the introduction of a new grade and a skills mix project for bottom-line savings.
19. These challenges and the company's position have been compounded by the JCRA's proposals and our members are now being put under huge pressure of compulsory redundancy by Jersey Post. It must be borne in mind that any decision to introduce competition into the bulk mail market or to cut the USO is, ultimately, making a trade-off against their jobs and terms and conditions. Again, we believe this strongly counts against the JCRA's proposals.
20. Even if the proposals to reduce the USO do not go as far as the Green Paper contemplates, we do not believe that introducing competition in the bulk mail market would have countervailing benefits to be weighed against the impact of the reductions in the core service this would lead to.
21. As we noted in our submission to the JCRA, Jersey enjoys two advantages with regard to the fulfilment market: firstly qualifying for the EU low-value consignment relief, which enables goods worth less than €10 to be imported into EU member states without VAT being charged; and secondly the memorandum of understanding between UK HMRC, Jersey Post and Royal Mail, which allows for the collection of UK VAT in Jersey, enabling imports to bypass UK customs controls, speeding up the importing process for mail.

22. The UK, which is the end destination of 90% of over 90% of the bulk mail from Jersey<sup>[7]</sup>, has opted to apply the relief to goods worth less than £18, roughly double the threshold required by the EU – and the maximum threshold permitted – and for UK Revenue and Customs this higher rate and the customs agreement with Jersey Post are trade-offs, weighing the lost tax revenue from imports from Jersey against the extra administrative costs the UK would face in dealing with a larger volume of goods.
23. With the cost of the arrangement being estimated to be around £110m<sup>[8]</sup> in lost tax revenue to the UK Treasury – £80m of which is estimated to come from the Channel Islands<sup>[9]</sup> – it is far from clear that there is potential for growth in Jersey's fulfilment industry. In 2006 as a result of political pressure in the UK, the Jersey States issued a policy notice introducing a licensing regime for fulfilment providers restricting growth in the sector and we note that on 13<sup>th</sup> July 2010 David Gauke MP, the Exchequer Secretary to the UK Treasury, stated that the Government was 'actively reviewing' the VAT relief arrangement.<sup>[10]</sup>
24. If the number of fulfilment providers in Jersey increased, it seems likely – particularly in the current financial climate – that the UK would seek to lower the VAT relief threshold, or alter the beneficial customs arrangements, which would significantly reduce the attraction of Jersey as a base for the industry. In light of the foregoing we cannot accept the JCRA's suggestion that granting new licences in the bulk mail market would be in the Island's economic interests.
25. Together with these doubts over the economic case for introducing competition, we do not believe that granting new mail licences in this sector would result in improvements for fulfilment providers. Firstly, Jersey Post already faces competition in this sector from other jurisdictions including Guernsey and Switzerland – both of which qualify for the European Union low value consignment relief scheme – and the UK, where businesses have direct access to Royal Mail's network.
26. Tesco recently relocated its fulfilment business from Jersey to Guernsey and the CWU understand that Jersey Post has lowered its prices to keep its business with Play.com, which had been in discussions with Swiss mail companies. It is clear from this that Jersey Post already faces competitive pressures requiring it to provide an efficient cost-effective service to fulfilment providers.
27. Secondly, reflecting this, the bulk mail service provided by Jersey Post is both high quality and competitive. In its 2008 consultation on Jersey Post's quality of service standards the JCRA noted that Jersey Post was considering introducing targets for its bulk mail performance. However the regulator recommended against doing so and stated that Jersey Post's sampling results for January and February of that year showed that 93% of bulk mail deliveries were completed within 3 working days. The consultation went on to note that Jersey

Post and Royal Mail agreed on a target of 87% of deliveries to be completed within 3 working days 'based on what *Royal Mail* feels *their network* can bear' – a target which the company met in 2009.

28. Thirdly in its last review of the business in 2007, the JCRA acknowledged that Jersey Post was an efficient operator and set the company a target of making £2.8m further savings by the end of 2010, which the CWU understands that the company is on course to meet. Jersey Post has announced further plans to make efficiency savings in 2010 beyond this and with an operating profit margin of only 1.4% in 2009 it is far from clear that the company is not offering fulfilment providers value for money.
29. In light of the foregoing, we believe that the economic context and the existing competition and standard of service for bulk mail providers undermine the JCRA's case for granting new licences in the bulk mail market in Jersey and that its main impact will be to damage both Jersey Post and the USO.

### **The roles of the JCRA, the Minister for Economic Development and the Minister for Treasury and Resources**

30. In accordance with article 8(1) of the Postal Services (Jersey) Law 2004 both the JCRA and the Minister for Economic Development have a primary duty to ensure that postal services – including the universal service – which satisfy all current and prospective demand are provided within Jersey having regard to the quality, affordability and accessibility of such provision for the highest number of users. Under article 8(2) the regulator and the Minister come under further secondary duties, to be discharged in line with article 8(1). [\[11\]](#)
31. For the reasons outlined in response to question 1 above, the CWU does not believe that the JCRA's decisions to grant licences to Citipost and Hub-Europe were in line with its primary obligation, with regard to the provision of a universal service under article 8(1) or that it made the correct judgment with regard to the promotion of Jersey's economic interests under article 8(2). Alongside the substantive objections we have to its final recommendations, we are also concerned about the JCRA's approach in reaching its decisions.
32. Firstly, the JCRA did not have a clear picture of the efficiency of Jersey Post but asserted that it had scope to make savings to contribute to the cost of the USO. The JCRA's last review into the efficiency of the business in 2007 found it to be an efficient postal operator and set further targets for the end of 2010, which it was on course to meet. The initial decision itself was published in April 2010, less than a month after the JCRA had initiated a tendering process for a new review, updating the 2007 study, to be completed throughout 2010. In light of these

facts it is unclear what evidence the JCRA had for its assertion and we believe that it should have had an up to date picture of the company's performance to inform its decisions.

33. Similarly the JCRA acknowledged that it was in disagreement with Jersey Post over the net-cost of the USO to the business and there was a gap of £4.85m between its last estimate (which put the cost at £100,000 - £150,000) and the current figures being quoted by the company (of a net cost of £5m). The JCRA made reference to 'significant work' which it had carried out on the cost of the USO, but did not publish this or disclose any estimate of the cost of the USO in its initial decisions. Such an assessment would clearly be germane to any evaluation of the likely impact of competition on Jersey Post in line with the JCRA's primary duty and, again, we believe the JCRA could not reach a properly informed decision without this information.
34. We also note that the JCRA's workplan for 2010 included a review into the scope of the USO. We believe that this should have been completed prior to its decisions, which will clearly have a material affect upon the service. Each of these points bring into question the JCRA's role and whether it is taking a truly objective approach to regulation. We are concerned that the JCRA may now feel the need to retrospectively justify its decisions to grant new licences in the bulk mail market in the work being carried out in 2010.
35. The CWU also believe that the JCRA misread the Hooper Report into the UK mail market, which it cited in support of its assertion that the benefits of competition are 'well known.' While we believe that this ignores the evidence of what has happened in the UK, it is unclear how the JCRA drew this conclusion from the report: the interim review from Hooper acknowledged that 'there have been no significant benefits from liberalisation for smaller businesses and domestic consumers' and the final report discussed only the *possibility* that such groups could benefit in the future. Again, this questions whether the JCRA is taking a truly objective approach to the evidence.
36. Given our belief that the JCRA failed to comply with its duties under article 8 of the Postal Services Law, we also believe that the Minister for Economic Development, who comes under the same duties for the protection of the USO, should have issued guidance to the regulator to reverse its initial decisions under article 9. We note that the Minister for Treasury and Resources wrote to the JCRA expressing concerns that the proposals to introduce competition would put the USO at 'serious risk' but that the Minister for Economic Development took no steps to address the issue.
37. As discussed in response to question 1, the Minister for Economic Development also published a Green Paper on the USO in June – after the JCRA's initial decisions regarding the bulk mail market had been published – proposing significant cuts to the universal service. The

CWU believes that this is a direct response to the likely impact of competition on the USO and, for the reasons raised in our response to question 1, we do not believe that these proposals are in the interests of the public, or businesses upon the Island.

38. Finally, we note that the Minister for Treasury and Resources has stated that he could not contemplate a situation where the company successfully obtains a public subsidy to meet its USO. We believe that it is a mistake to rule out public funding for a socially and economically beneficial public service which would not be provided by the private sector and we note that millions of pounds were taken out of the Jersey Post Office by the States of Jersey throughout the 1990s. Jersey Post itself was also incorporated as a company with a debt of £4m to the States in 2006 to cover pre-existing pensions liabilities which it paid to the States in 2007.
39. As with the JCRA's decisions to introduce competition in the bulk mail market, it is clear that the transfer of funds from Jersey Post to the States has a direct impact on its ability to continue to provide the USO. We therefore believe it is wrong to present the proposals to cut the postal service as the result of declining mail volumes and not the consequence of the States' past policies towards the mail service.

### **The performance and efficiency of Jersey Post**

40. The information which is publicly available indicates that Jersey Post delivers a good service to customers at a competitive price. In its last consultation regarding Jersey Post's quality of service in 2008, the JCRA's figures showed that in 2007 it was meeting two of its five delivery time targets. For 2009 Jersey Post has reported that all of these targets were met and that it exceeded its internal efficiency and customer targets over the same period. [\[12\]](#)
41. Furthermore the services offered are affordable, with all priority local letter and packet prices cheaper than the first class equivalent for Royal Mail. All European letters up to 100g are also cheaper than Royal Mail and Guernsey Post equivalents. [\[13\]](#)
42. We believe that this reflects the efficiency of the company and, as noted above, the JCRA's last assessment of Jersey Post's performance in 2007 evaluated it as an efficient operator. The CWU understand that it is on course to meet a further £2.8m of cost savings targeted by the JCRA at that time for the end of 2010 and we are currently working with Jersey Post on a number of measures to increase the efficiency of the business.

### **The Postal Services Law 2004 and the Competition Law 2005**



43. As discussed in response to question 2, under the Postal Services Law the JCRA and the Minister for Economic Development have a duty to maintain the provision of a universal postal service which is set out in Guidance issued by the Economic Development Committee in 2005. We believe that the moves by the JCRA to introduce competition in the Jersey bulk mail market are not in line with this duty, as is already enshrined in the Law.
44. However, we believe that more explicit stipulation of the JCRA's duty to safeguard the universal service in the Postal Services Law, would direct the regulator towards this task more effectively. Furthermore, this would require any amendments to the universal service to be made through the legislative procedure, which we believe is of fundamental importance for any changes being made to a basic public service, as opposed to guidance issued from the Minister.

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[1] Jersey Post Business Review 2009

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

[3] Jersey Post Annual Report 2008. It is not clear whether the estimated impact of competition in Jersey related to operating profit (£4.3m) or total profit before taxation (almost £6m).

[4] For the majority of users in the UK the introduction of competition has led to price increases and declines in service, with fewer deliveries, fewer collections and later delivery times.

[5] This claim is made on page 8, paragraph 4.8

[6] At the end of 2009 from 6,070 active undertakings 2,660 of these were single-person operations. With regard to employment, 24% of jobs were in the finance sector with 16% in retail. Jersey Labour Market at December 2009, States of Jersey Statistics Unit.

[7] JCRA consultation on Jersey Post's Quality of Service, 2008.

[8] The figure was given by Stephen Timms, then Financial Secretary to the Treasury, in a Westminster Hall debate on the low-value consignment VAT relief on 27/1/2009.

[9] This amount was given by Stephen Timms in response to a written question on 12/2/2009.

[10] This statement was given in answer to a written question – see Hansard, House of Commons debates 13 July 2010, column 661W.

[11] These include promoting competition where it would be in the interests of postal users, encouraging efficiency, furthering the economic interests of Jersey, limiting restrictions on service providers and ensuring they have sufficient resources, and having regard to disabled persons or those with limited financial resources or particular needs.

[12] See <http://www.jerseypost.com/aboutus/OoS/Pages/Monitoringandsuccess.aspx> and the Jersey Post Business Review 2009. We note that Jersey Post's delivery targets are comparable to Guernsey Post (GP), with all of them within one percentage point of GP's figure, with the exception of Guernsey – Jersey mail (88% for GP and 84% for Jersey Post respectively) and bulk mail, for which GP negotiates targets with individual mailers.

[13] Based on performance figures and prices published in Jersey Post's size-based pricing application, February 2010.