

POSTWATCH RESPONSE TO POSTCOMM'S CONSULTATION ON ROYAL MAIL'S SPECIAL PRIVILEGES

Introduction

1. Postwatch welcomes the opportunity to comment on Postcomm 's consultation on Royal Mail's special privileges. The review is necessary to ensure that Royal Mail does not have an unfair advantage over its competitors through the use of these privileges but that any necessary for the provision of the universal service are maintained.

Timing

2. We note that all the privileges outlined in this consultation are statutory and hence outside Postcomm's remit. Consequently, at the end of the consultation Postcomm will have to make recommendations to relevant Government departments if it wishes to abolish, extend or limit any privilege. We urge Postcomm to outline in any publication following this consultation its proposed timetable for seeking legislative changes as it is unclear how long this process will take and how it will tie in with forthcoming Postcomm decisions, such as the next stage of market opening.

Postcomm's Approach

3. Whilst Postcomm has focused solely on the statutory privileges enjoyed by Royal Mail. Postwatch believe that there may be other advantages which could be interpreted as privileges. We elaborate further on this below.
4. In addition we believe that Postcomm's analysis does not take into sufficient account the need to level the playing field now in order to allow competition to develop. A privilege, which may not be a barrier to entry at the moment could distort competition in the future and should be removed without delay provided it is not necessary for the provision of a universal service.
5. Postcomm also appears to make the assumption that Royal Mail will always be the sole universal service provider and does not allow for the possibility that in the future there may be other universal service providers (possibly within limited geographical areas). We urge Postcomm to make provision to extend any privileges to all future universal service providers.
6. Consequently, whilst Postcomm's four box approach is a perfectly valid and useful way of categorising possible outcomes it must not constrain the result. For example, although there may be a case for removing a particular privilege there are elements within some privileges, such as power to make schemes and compulsory right to purchase land that may be worthwhile retaining or revisiting as their immediate removal may impact on the universal service obligation. Postwatch has found some difficulty in fitting its recommendations into the boxes as we propose that some privileges be modified and some extended in part.

Statutory Privileges

VAT

7. We believe that this is the most significant of all Royal Mail's privileges and must be tackled immediately in light of the fact that the VAT exemption works against Postcomm's market opening strategy by closing off to competition a significant proportion of the 30% of the market which Postcomm opened to competition at the beginning of last year.
8. We recognise that this is an issue that can only be resolved at European level as it requires an amendment to the 6th VAT Directive. In this regard we were pleased that the European Commission put forward proposals attempting to level the playing field last May. These appeared to provide a sensible starting point for discussion but we have been disappointed that more progress has not been made.
9. We believe Postcomm's modelling work is an important contribution to the debate in the UK as it illustrates the impact of both applying VAT at 17.5% on all services and a 5% reduced rate on standard addressed postal items under 2kg (17.5% on all other services).
10. We agree with Postcomm that the exemption is not necessary for the provision of the universal service and that there is no justification for Parcelforce to continue to benefit from the VAT exemption.
11. Postwatch's current position is that the VAT playing field should be levelled. In order to do so we do not support applying VAT at 17.5%. The application of a reduced rate is one possible solution but it should not increase the price of stamps. Any solution to this issue must also take into account the impact on organisations such as charities that cannot re-claim VAT. This could be achieved either by either facilitating a re-claim of their VAT or if a reduced rate is applied construing the definition of standard postal services in a sufficiently broad manner to capture items posted by charities. We are also highly conscious that there will be major practical difficulties in calculating and collecting VAT payable if different items and payment channels are subject to a different regime.
12. It appears that the Government's current position on this issue is at odds with Postcomm's market opening strategy and it would be helpful if this conflict could be resolved, particularly with the second phase of market opening in prospect. If this proves impossible, Postcomm may wish to reconsider its liberalisation strategy and open a significantly larger part of the market to competition in 2005 (perhaps 100%) in order to compensate for Royal Mail's inherent tax advantage.

Customs Clearance Procedural Regulations

13. Postcomm identifies the privilege for debate as the use of simplified customs declarations by Royal Mail as a universal service provider. On the basis of the information provided it is difficult to see the consequences of particular choices, particularly their effect on the position of Parcelforce. It may have been better to consider the privilege in terms of the traffic streams to which it applies, identifying commensurate traffic streams and considering these together. On this basis inbound international parcels delivered by Parcelforce appear like those delivered by Royal Mail (no distinction being necessary on universal service grounds). Like Royal Mail Parcel Force does not have control over what is posted in another country. This distinguishes

it from operators such as FedEx and creates an argument that decisions on the exemption for Royal Mail should also be applied to Parcelforce. Postcomm have not exposed this issue.

14. Similarly, we do not believe Postcomm has fully exposed the nature of the privilege in that Royal Mail also benefits from using Customs and Excise officials to calculate duty or other taxes owing while other operators must make this calculation themselves and bear the cost. This affords Royal Mail a competitive advantage.
15. Postcomm states that Royal Mail derives a competitive advantage from not having to complete time consuming and complex import/export documentation. This may be true, however, the procedures used by other operators may actually facilitate the smooth flow of international mail to receiving customers upon arrival in the UK. Although posting customers in other countries using private carriers to post items to the UK must provide a full customs declaration, the information is captured electronically making it easier to identify problem packets and calculate the duty to be paid. Posting customers sending universal service items for delivery by Royal Mail provide data in written form that must be extracted manually, potentially delaying the onward delivery of items by Royal Mail.
16. We therefore believe that the 'privilege' lies not so much in the simplified procedures but in the fact that Royal Mail can avail itself of Customs and Excise staff to calculate the duty payable. In the case of universal service postal items this may indeed be necessary to facilitate the calculation of duty (which must happen before delivery). However, for non-universal service items Royal Mail should be responsible for the calculation of duty in the same manner as other operators. In this regard we note that the European Commission has put forward proposals to bring the procedures applicable to public postal providers more into line with those applicable to private operators and we await the outcome of this initiative.

Exemption from Traffic Regulations

17. Postwatch believes that this exemption provides a significant advantage to Royal Mail. Our view is that the only unique aspect to the Universal Service Obligation relying on this privilege is the collection of mail from pillar-boxes. Postwatch therefore argue that this privilege should only apply to collections from pillar-boxes. It should, however, be extended to all universal service providers. As for all other types of collections and deliveries, Royal Mail should rely on general waiting and loading exemptions or make use of car parks, etc. like all other operators.
5. While it can be argued that the existing privilege enables Royal Mail to carry out its Universal Service Obligation role, it also appears to distort competition as it gives Royal Mail greater flexibility in organising its collections and deliveries. Other operators have to rely on general waiting and loading exemptions, which permit vehicles to stop on yellow lines to load/unload items for a limited amount of time. Further to this any additional costs on other operators incurred due to parking fees and manpower could provide a competitive disadvantage. We understand that such loading exemptions, although they vary, can be for periods of 20-30 minutes and we believe such time frames should be sufficient for Royal Mail purposes to properly carry out its Universal Service Obligation.
6. Postwatch agrees with Postcomm that, as Parcelforce no longer provides any part of the Universal Service Obligation, there is no justification for it to benefit from Royal Mail's parking privileges.

7. Due to the differing approaches taken by local authorities in this area Postcomm might also consider providing guidance to local authorities as to how distortions to competition might be minimised. It should be noted that any changes to the current regime would need to take account of local traffic authorities' desire to keep traffic congestion to a minimum.

Carriage of Mailbags by Ship and Aircraft

8. The carriage of mailbags by ship and aircraft does not appear to be a significant barrier to competition. Postwatch agrees that it might not be necessary to keep this privilege as it does not seem to be relevant today and Royal Mail should be able to enter into commercial negotiation for the transport of mail to any outlying areas. However we do not accept Postcomm's reasoning that it should be abolished simply because it has not been used recently.
9. Presumably Royal Mail is already paying commercial rates for carriage of universal service mail on ships and aircraft. Hence there does not seem to be any reason for keeping this privilege.

Harbour Legislation

12. As above, we do not accept the argument that it should be abolished simply because it has not been used recently. We agree that Royal Mail does not necessarily need this privilege, as it should be able to reach appropriate agreements with harbour authorities on these matters. However, we believe it would be useful to keep this privilege in order to prevent harbour authorities from detaining universal service mail. This would act as a safeguard if the authorities decided to increase harbour fees unreasonably. Such a privilege could be particularly important for providing a universal service to remote islands where deliveries can only be made via one particular harbour.

Immunity from Prosecution

14. Postwatch believe there is no compelling case for this privilege on universal service grounds alone. We have difficulty with the argument that universal service mail is unique compared to the mail of other operators. The only mail that Royal Mail does not have any control over is mail posted in pillar-boxes. We therefore argue that this privilege should be retained only for pillar-box mail and that it should be extended to all universal service providers. It seems that for all other postings Royal Mail has as much control over what is being posted as the other operators.
15. Royal Mail's competitors are subject to prosecution for carrying prohibited articles, while Royal Mail is not. Other operators have to have systems in place to check that they do not carry prohibited items, which is likely to impose additional costs and potentially distort competition.

Compulsory Purchase Powers

19. Postwatch note that this power is rarely used and therefore its importance for carrying out Universal Service Obligation and its potential to distort competition are theoretical. We agree with Postcomm that there is no compelling case to retain the compulsory purchase element of this privilege and it is probably not necessary to keep it, as the universal service provider should be able to employ normal commercial means to obtain land.

20. However, it also enables Royal Mail to acquire easements or rights over land, which could be important for the purpose of securing access to operational premises. The nature of this is unclear from Postcomm's consultation paper but we believe that this could have, albeit in limited circumstances, an impact on Royal Mail's ability to carry out its universal service obligation. Postwatch believe that there is a case for separating this 'privilege' and exposing the easement element to further analysis as it is unclear whether the consequence to removing it would impact on Royal Mail's ability to carry out its universal service obligation.

Provision Relating to Public Pillar Boxes

23. Postwatch consider this privilege to be necessary for the provision of the Universal Service Obligation as pillar-boxes provide a simple and convenient means to provide the service. Pouch boxes also appear desirable for provision of the universal service. Further, in its current form this privilege does not seem to distort competition.

24. However, in future other operators may wish to offer services requiring the provision of public pillar-boxes. Consequently, Postwatch believe that this privilege should be extended to all operators wishing to establish pillar-box networks. We acknowledge the fact that Postcomm has allowed for the possibility for this privilege to be extended to other operators in due course as it might take considerable time to change this privilege and in its current form it could act as a barrier to entry and limit the development of competition.

Classification of Royal Mail as a Private Carrier

29. Postcomm's provisional view is that this statutory provision is not a privilege as such and that it does not appear to distort competition. Postcomm therefore suggests that RM should retain this privilege in relation to its classification as a private carrier. However, we are unable to form a view without further understanding why removing this classification would be incompatible with RM's universal service obligations. The current consultation makes this assertion but does not provide a rationale.

30. We are also unsure whether Royal Mail's classification as a private carrier affords distinct rights separate from those provided by Royal Mail's ability to make schemes and in particular section 90 of the Act on exclusion of liability. We ask Postcomm to clarify whether there is any overlap here and if so how this impacts on the analysis.

31. In any case, if retained, it seems illogical that this privilege should be extended to all universal service providers not just RM.

The Power to make Schemes

32. The power to make schemes relates to sections 89-92 of the PSA and section 93 which enables the Secretary of State to modify these statutory provisions following a consultation with Postcomm and Postwatch. Postcomm states that it has not addressed this privilege because Postwatch and Postcomm have already raised with the DTI the case for reviewing these provisions of the Act. However, we understand that the current discussion with the DTI relates to 'Exclusion of liability' (Sections 90-92 of the PSA) in the context of compensation. This discussion does not directly cover Section 89 ('Schemes as to terms and conditions for provision of a universal postal service') and it is unclear why Postcomm has not included this in its consultation document.

33. Without prejudice to the outcome of discussions with DTI our view is that the power to make schemes is important to universal service providers in providing 'terms and conditions' for customers without entering into individual contracts with everyone who

uses the postal system. Consequently, this power should be extended to all universal service providers.

Other privileges and barriers to entry

35. Postwatch has identified several other non-statutory privileges enjoyed by Royal Mail not covered in the consultation document. These could fall under the heading of privileges afforded to Royal Mail as a result of its former monopoly status. These include exemptions from the Working Time Directive and Health and Safety Legislation, the ability to issue stamps with the Queen's image, the fact that only Royal Mail may license franking machine suppliers, and ownership of PAF. There may be many others.
36. It appears to us that all of these advantages are privileges that could potentially give Royal Mail a competitive advantage and Postcomm could usefully have considered them in this consultation. Postcomm may now wish to outline when it proposes to review such non-statutory privileges.
37. In its recent Market report Postcomm identified a number of barriers to entry and asked respondents how significant these are and whether Postcomm has identified all the barriers. There is no doubt that the issues Postcomm has identified are barriers to entry but it is difficult to evaluate their importance given their intangible nature.
38. Postcomm's figures illustrate that Royal Mail currently has 99.75% market share despite 30% of the market being opened to competition. Consequently, we believe that consumers would benefit if Postcomm developed and outlined a program to actively tackle both statutory special privileges, privileges afforded to Royal Mail as a result of its former monopoly status, and barriers to entry.