

Special Mail Services Ltd

To the Postal Services Commission

Revised Market Opening Timetable, Proposals for Consultation, September 2004

Introduction

1. Thank you for the opportunity to contribute to Postcomm's Proposals for consultation on its Revised Market Opening Timetable.
2. Special Mail Services Ltd is a private postal operator that provides end-to-end services for the secure delivery of valuable items. We are also substantial users of Royal Mail services. Although we do not currently operate within the licensed sector of the postal market we are in every sense truly active in the postal market and are affected by Postcomm's decisions about the future of the market. Furthermore, our own strategic plans will be directly influenced by the future regulatory environment.
3. We would firstly like to note that this consultation is only one of several that are currently ongoing, many of which have the same submission date. All of these consultations are extremely detailed and several are very technical and we fear that Postcomm is not providing sufficient time and opportunities for stakeholders to develop an understanding of the issues and respond in a fully informed manner. We would like to receive an assurance from Postcomm that in future it will pay more attention to the number of consultations that are being launched by Postwatch and itself and phase these launches and submission dates to reduce the load on consultees.

Market Dynamics

4. We welcome Postcomm's proposal to accelerate market liberalisation. In other countries which have introduced full competition and in which the dominant incumbent operator has already been efficient it is evident that competition has been very slow to develop and the incumbent has maintained extremely high market shares. We see no reason why this should be any different in the UK and we are glad that Postcomm is now introducing measures that should have been introduced several years ago. We urge Postcomm to proceed with full market opening with effect from 1 January 2006, if not sooner. Anything less than full market opening will be ineffectual.
5. We perceive that Postcomm's liberalisation timetable has been unduly influenced by Royal Mail's interests and hope that these new measures mark a turning point in this behaviour.

6. We wish to draw Postcomm's attention to the fact that the UK postal market is already characterised by services that, in international comparison, are largely already very high quality and low price. Even with the new market opening measures it will be very difficult for competitors to enter the market to any significant extent.
7. This is particularly true as long as Royal Mail benefits from special privileges such as the treatment of its VAT.
8. We believe that Postcomm is greatly underestimating the difficulty of competitive market entry and we believe that significant small scale local entry will not happen to the levels claimed by Royal Mail. In any case, the fact that will be market exit is irrelevant. Market exit is a vital feature of vibrant market economies and customers have a more sophisticated appreciation of these matters than Royal Mail would have you believe. Postcomm's licensing regime provides customer protection in the event of an operator leaving the market.

Licensing

9. We fully support the continuation of licensing in a fully liberalised postal market although we have considerable misgivings about the nature of the licences Postcomm is proposing.
10. In essence, we believe that Postcomm is considerably overestimating the necessity for it to oversee the regulation of mail integrity above and beyond the level specified in the Postal Services Act. The result of this error is a proposed licensing regime that will interfere in the internal organisation and operation of new entrant postal services and will form a substantial barrier to market entry. From the evidence that we have heard and seen so far there is little about Postcomm's proposed licences that can be described as "light-touch".
11. We wish to draw to Postcomm's notice the fact that there are already two end-to-end postal companies operating in direct competition to Royal Mail. These are Special Mail Services and DX Network Service. Both of these companies provide postal services to customers with highly exacting demands on mail integrity. Both of these companies meet the customer requirements for mail integrity of their own free will because their services are almost wholly exempted from the requirement to be licensed.
12. We also wish to draw Postcomm's attention to the fact that there is a massive express services industry carrying, by and large, extremely valuable items and that this industry is unregulated.
13. We recommend that Postcomm take a closer look at the licensing regimes in countries such as Germany, Sweden and New Zealand.

None of these countries has experienced a collapse in confidence in postal services even though they all have licensing regimes that are far less regulated than Postcomm's proposals.

14. We will address these matters in greater detail in our response to Postcomm's licensing consultation.

Price Control

15. We note that Postcomm has launched its Consultation on Principles for the 2006 Royal Mail Price and Service Quality Review in parallel with this consultation. We have made a separate submission to that consultation. The main concern expressed in that submission is that Postcomm's price and quality strategy will restrict the opportunities for competitors to enter the market and result in the continuation of the current 'one size fits all' postal service. We appeal to Postcomm to allow Royal Mail greater commercial freedom to agree quality levels with its customers.
16. We acknowledge that prices in a fully competitive market will be reflective of underlying costs and we can understand Royal Mail's desire to rebalance its prices. However, we have two grave concerns. The first is about the reliability of Royal Mail's costing systems and their ability to allocate costs. The second is about the desirability of prices reflecting Royal Mail's existing costs. In the case of the move to size based pricing it is evident that Royal Mail has failed to invest in the equipment needed to serve the current market with the result that it now wishes to turn the market's tariff structure on its head in order to shoehorn customers into compliance with its unsuitable processing capabilities. In the case of major price adjustments such as the introduction of size based pricing we believe that it is essential for Postcomm to undertake a full cost/benefit analysis, considering all of the additional costs incurred by the mailing industry, before approving the change.

Universal Service

17. We are concerned about Postcomm's proposal to define Mailsort 1400 as the generic universal service product for bulk mailers. Mailsort 1400 requires mailers to sort their mail to a very detailed level and is only attractive to the largest, most sophisticated mailers. Excluding other bulk mail products from the universal service would prevent the vast majority of mailers benefiting from these services. There is also evidence that Royal Mail is, counter-intuitively, trying to convert Mailsort 1400 users to Mailsort 120. We also fail to understand how Postcomm could exclude Cleanmail from the universal service. Cleanmail is a product that requires no presorting. Most Cleanmail users will not be able to provide Royal Mail with destination details for

mail carried under this tariff and so it is not possible for this product to be subject to geographically de-averaged pricing.

We are confused by Postcomm's thinking about bulk mail and access products. In essence, all of these products are examples of worksharing. We see no reason why any of these products should be subject to geographically de-averaged pricing. It seems perverse that Royal Mail would wish to undermine its own ability to finance the universal service in this way.

Even the use of access products by operators is only an instance of worksharing and there is no justification for discriminating against access operators. There is no fundamental difference between the activities of an access operator and those of a mailhouse.

We note that the requirement for downstream access to Royal Mail's pipeline was required in order to facilitate the entry of end-to-end operators into the market. To date entry into the end-to-end sector has been limited to two operators, neither of which has negotiated access contracts. The removal of access products from the universal service is a pre-emptive move on the part of Royal Mail to frustrate market entry by potential competitors.

Once again we wish to stress the importance of Postcomm convincing itself about the reliability of Royal Mail's costing data before contemplating a relaxation of the requirement for geographically uniform pricing.

Other Matters

18. We welcome Postcomm's proposals to increase market awareness. We wonder if it would be possible for operators to participate in Postcomm's regional roadshows.
19. We welcome Postcomm's proposed measures regarding market infrastructure development. We wish to draw Postcomm's attention to the need to consider transport equipment (e.g. cages and trays) within this work.
20. Finally, we urge Postcomm in this consultation, as we have done elsewhere, to broaden its view of the postal market. Postcomm is responsible for regulating the whole of the postal market, both licensed and unlicensed, and its research and analysis need to reflect the fact that operators such as Special Mail Services and DX Network Services are already active in the market, providing postal services to mail users in direct competition with Royal Mail. We believe that in failing to identify this activity in its analysis Postcomm is unwittingly perpetuating the impression that this is no competition and reinforcing customer inertia.

21. If you would like to discuss any of these points in greater detail please contact:

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