

Consumer Focus submission

Royal Mail's application to introduce a Sustainable Mail product – Postcomm consultation

March 2009

Postcomm Consultation: Royal Mail's application to introduce a Sustainable Mail product

Recommendations

Consumer Focus recommends that:

- The Sustainable Mail Retail product is included in the Price Control.
- Postcomm modify Licence Condition 21(5) to allow Royal Mail to maintain a minimum level of headroom between 'like for like' access and retail products.
- The regulator conducts a review of the current access arrangements as a priority.

Background

1. Consumer Focus is the new statutory organisation campaigning for a fair deal for consumers in England, Wales, Scotland, and, for postal services, Northern Ireland. We are the voice of the consumer and work to secure a fair deal on their behalf. We were created through the merger of three consumer organisations – Postwatch, energywatch and the National Consumer Council (including the Welsh and Scottish Consumer Councils). The new approach allows for more joined-up consumer advocacy, with a single organisation speaking with a powerful voice and able to more readily bring cross-sector expertise to issues of concern.

Sustainability

2. Consumer Focus welcomes any attempts by organisations to promote and/or introduce products and services which allow consumers to make choices which are consistent with sustainable living. We are therefore encouraged by Royal Mail's efforts to introduce products and services which aim to meet this objective. We have not discussed the environmental credentials of the Sustainable Mail product in this consultation response but rather discuss, as requested by Postcomm, the proposed changes to the regulatory framework. However, we would welcome the opportunity to offer Royal Mail the consumer perspective in any sustainable products or services they intend to launch in future.

Outline

3. The outline of the document responds to the three main options/decisions Postcomm discuss in their Consultation document, these being:
 - Whether the Sustainable Mail product should be included in the Price Control;
 - Whether the Sustainable Mail product should be set as the Access Reference Point in Condition 21(5) and;
 - Whether the Sustainable Mail product should be introduced as part of a modified Access Headroom arrangement.

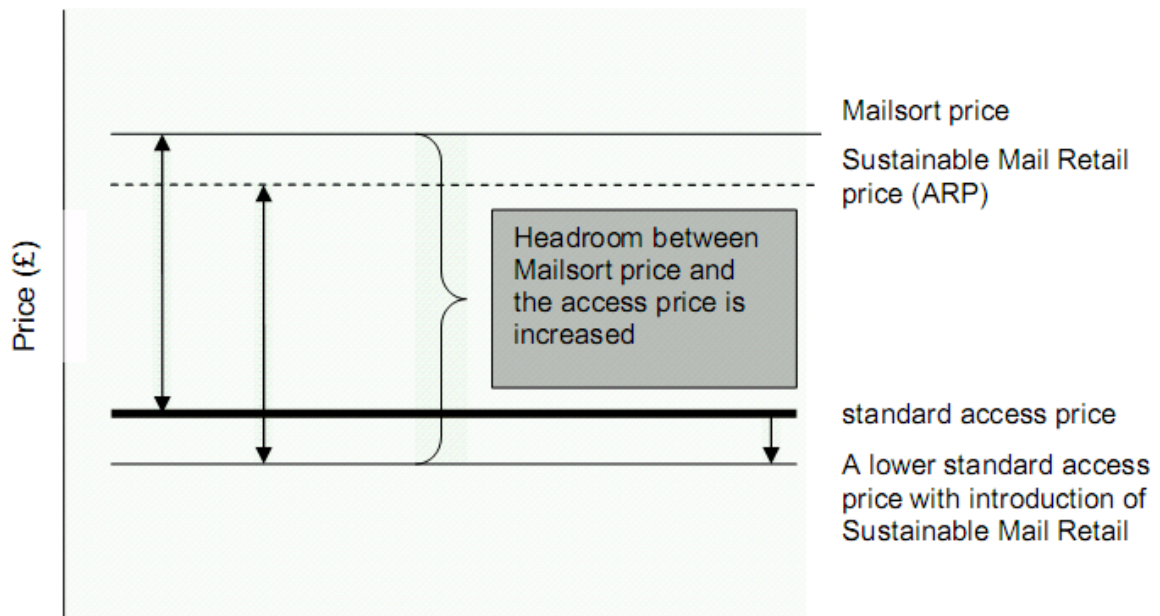
4. Our thoughts and recommendations on each of these questions are below.

Should Sustainable Mail Retail (SMR) be included in the Price Control?

5. Under Licence Condition 21 a new product or service will form part of the price control if it is deemed to be substantially similar to an existing controlled service. SMR is different in two respects to a 'normal' bulk mail product:
 - The customer is required to use 'green' materials and ensure these materials are recyclable.
 - The customer is required to ensure that its internal mailing list is kept up to date and that it applies a direct mail opt out system.
6. Consumer Focus is satisfied with the criteria adopted by Postcomm to determine whether or not the SMR product is substantially similar to other controlled services. Furthermore, we are in agreement with Postcomm's analysis of the SMR product in that the product is substantially similar to existing controlled services.
7. Consumer Focus believes that the SMR product does not exhibit any new innovations in terms of reducing production costs or providing a more secure service. It does provide an incentive structure which the customer is required to meet. However, the incentive system seen in other mail products, such as Mailsort, rewards discounts for greater volumes of mail sent. The new incentive structure, which separates the SMR product from other Royal Mail products, rewards discounts for meeting environmental criteria. In effect both bulk mail products (Mailsort and SMR) are the same, only the criterion by which a customer can receive a discount, albeit a greater one, is different.
8. Consumer Focus believes that it is essential that postal products which share substantially the same characteristics as existing controlled services be retained within the Price Control, as this provides valuable protection for consumers from a dominant firm, in this case Royal Mail, exploiting its position to the detriment of consumers where competition is not strong enough to impose competitive pressures on the dominant firm.

Should SMR be set as the Access Reference Point in Condition 21(5) (headroom arrangement)?

9. Postcomm has said that for the SMR product to comply with Condition 21(5) and maintain a minimum level of headroom between the standard access price and the set Access Reference Price (ARP), the SMR product would have to be set as the ARP and would be used as the point at which the minimum level of headroom would have to be maintained with the standard access price. Figure 1 below illustrates his scenario:

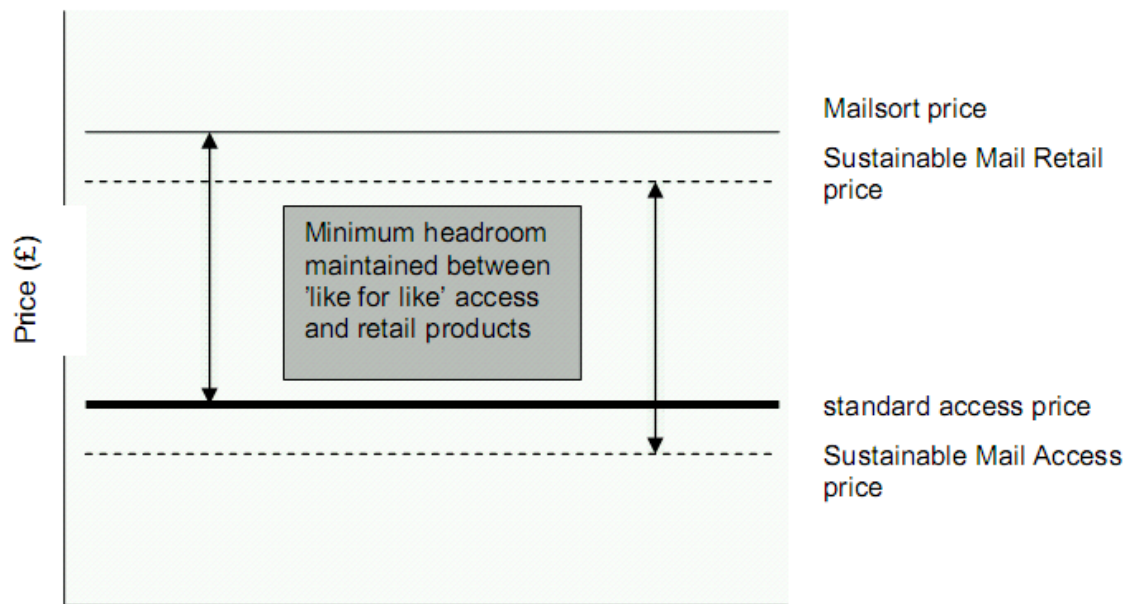


Source: Royal Mail's application to introduce a Sustainable Mail product Consultation, Postcomm (February 2009) p.11

10. Consumer Focus is in agreement with Postcomm that this would create an unfair market distortion which would penalise Royal Mail. There would be a disincentive to provide a sustainable mail product as Royal Mail would need to make changes to the pricing levels of other products they offer which have the potential to benefit their competitors' revenue streams or have an adverse effect on Royal Mail's revenue and/or volume levels. These potential adverse effects would not improve Royal Mail's current financial state, especially as mail volumes are predicted to deteriorate in the next few years. Just recently Royal Mail's Chief Executive, Adam Crozier, told the Business and Enterprise Select Committee (24 February 2009 – uncorrected oral evidence) he expected mail volumes to drop by 8% in 2009. Placing Royal Mail at a competitive disadvantage to its competitors may further compound the problems Royal Mail already face, putting the provision of the current USO at risk.

Should SMR be introduced as part of a modified Access Headroom arrangement?

11. For the reasons articulated above Consumer Focus supports the solution proposed by Postcomm which would in our view allow for a more balanced outcome in terms of the benefits accruing and the disadvantages placed upon Royal Mail and its competitors. This solution is illustrated in Figure 2 below:



Source: Royal Mail's application to introduce a Sustainable Mail product Consultation, Postcomm (February 2009) p.15

12. We therefore fully support Postcomm's proposal that Condition 21(5) of Royal Mail's licence be modified to require Royal Mail to maintain a minimum level of headroom between 'like for like' access and retail products i.e. in this case minimum headroom required for sustainable mail products *only*.
13. We believe this measure will be to the benefit of consumers in the short to medium term for the following reasons:
 - It will minimise the disincentive to Royal Mail of introducing a sustainable mail product and stop Royal Mail's competitors having a free reign in supplying an explicit environmentally friendly product. Such a situation could have a negative impact on Royal Mail's revenue and mail volumes which could place the current universal service at risk.
 - In the consultation response Postcomm refer to the voluntary agreement struck between the government and the Direct Marketing Association (DMA) to increase the level of recycling of direct mail. We are concerned to hear that Defra will consider implementing alternative measures, such as an opt in direct mail scheme, if the environmental targets are not met.

Consumer Focus supports measures, such as Royal Mail's Opt out Service, which give consumers a choice of whether they wish to receive direct mail. These services must give clear guidance about what mail consumers will *not* continue to receive and must also allow important government and public information to be continued to be delivered. For example consumers must still be guaranteed to receive electoral roll and public health and sanitation information. However we would not be in favour of a direct mail opt in

scheme. If such a scheme was implemented by the government we believe this would have the effect of speeding up the rate of decreasing mail volume, putting further financial pressures on Royal Mail, placing the current universal service at risk. By allowing Royal Mail to introduce a sustainable mail product we believe this it is more likely that the DMA will meet its targets preventing Defra from imposing a potentially damaging scheme upon the mail market.

Review of the current access regime

14. However, while Consumer Focus believes this is a satisfactory short to medium term measure, it does not provide a permanent solution to the issues surrounding the access regime.
15. While we understand the logic behind Condition 21(5) which prevents Royal Mail from indulging in ‘margin squeeze’ which would constitute an anti competitive act which would be to the detriment of consumers, we believe that as a priority the regulator should undertake an immediate review of the current access arrangements to determine whether this form of competition actually benefits consumers and the universal service, or in fact inhibits end-to-end competition and/or places Royal Mail at a competitive disadvantage to their competitors, which may threaten the universal service.
16. We would expect the new regulator to undertake an exercise as outlined in the Hooper report. This would review three main aspects of the access regime:
 - Whether the headroom margin is related to Royal Mail’s costs.
 - Whether the access regime dilutes the incentives for Royal Mail to become more efficient.
 - Whether Royal Mail is providing access services at a loss or profit.¹
17. The consultation document outlines the possible issues surrounding cost reflective products, rebalancing effects in terms of lower prices for larger companies in comparison with smaller companies and the possibility of inhibiting the development of end to end competition. While these issues are relevant to this consultation document we believe these questions can be better answered and have better solutions proposed in the context of a more general consultation on the current access regime.

¹ Modernise or Decline – Policies to maintain the universal postal service in the United Kingdom, (the Hooper Report) (16 December 2008) p.98