

## III.2-7: Postcomm, the British Postal Services Commission, publishes a new regulatory framework for a sustainable postal service on May 27, 2010.

Tuesday 22 June 2010, by Alex Raiffe, Junior Editor

### MAIN INFORMATION

Through the publication of a new regulatory framework by Postcomm, the British Postal Services Commission, on May 27, 2010, Postcomm outlines its plans for regulating the postal sector in the years following 2012. This framework plans to adapt postal regulation to allow Royal Mail to profitably fulfill its Universal Service Obligations faced with drastically declining mail volumes and increased competition.

### CONTEXT AND SUMMARY

The current regulatory framework for postal services in Britain has been in place since January 1, 2006, when the British postal services market was entirely opened to full competition.

This framework was introduced at a time when Postcomm predicted that mail volumes would continue to grow, and could not yet predict the level of competition that would exist on the market.

The current framework is now seen as too restrictive, and Postcomm intends to shift postal regulation away from sector-specific regulation, and towards general Competition Law.

This document's principle goal is to use sector-specific postal regulation **only** where required to (i) maintain universal postal service, (ii) maintain competition in areas where *Royal Mail* is in a dominant market position.

In order to achieve this goal, Postcomm plans for:

- The substantial deregulation of parcel service based on weight and volume
  - o It has been concluded that *Royal Mail* retains a dominant position only within the market for parcel items sent by consumers from postal collection points (post offices), and for low-weight (>1Kg) packets sent by business with low volumes of packets sent.
  - o Therefore, price regulation would be removed from express parcel services sent by businesses.
  - o Price regulation would be removed from regular parcel services sent by businesses for (i) packets above 750g; (ii) high-volume consignments with average weight above 1Kg per packet; (iii) any consignment with an average weight above 2kg.
  - o This would allow *Royal Mail* to freely set and negotiate prices in the above service categories.
  
- Partial deregulation of pre-sorted bulk mail
  - o *Royal Mail* has a dominant market position in all categories (pre-sorted, unsorted bulk, and unsorted individual letters) and all levels of service (priority and economy<sup>[1]</sup>). However, competition is increasing for pre-sorted and unsorted bulk economy mail.
  - o any of *Royal Mail's* competitors rely on *Royal Mail's* inward sorting and delivery facilities to provide service.
  - o In order to foster competition, **retail** price caps would be removed from bulk mail services, but would be replaced with **wholesale** price cap rates. This would allow *Royal Mail* to freely fix rates charged to consumers, but maintain a regulated price for charging competitors. This would foster competition by allowing *Royal Mail* to compete for consumers by pricing, but would prevent it from evincing competitors by predatory wholesale pricing by maintaining fixed prices for access to its facilities.

- Changes to “headroom” and improved competitor access to facilities
  - o Associated with the change from retail to wholesale price caps is a change in headroom control, which is the amount of price reduction that *Royal Mail* is required to accord competitors using its facilities, in order to allow them to compete on retail pricing.
  - o Postcomm would expand the range of products subject to headroom control.
  - o Postcomm would remove explicit headroom control per product (in other words, there would no longer be a specific discount per product).
  - o Explicit headroom control would be replaced by a “basket”, in which *Royal Mail* would be able to freely fix its amount of headroom–per–product itself, within a range, and with the obligation of maintaining a general percentage of headroom.
  - o Elements of packets and parcel service would be completely deregulated, allowing *Royal Mail* to freely set prices for these services in a competitive market.

- Roll–over of other features of price controls
  - o Stamps and unsorted bulk mail would remain subject to current price controls
  - o Prices for small customers rise at an average of inflation rates minus 0.14%; prices for business customers rise at an average of inflation minus 1.96%. Individual services have a 3% flexibility, as long as overall pricing does not exceed the aforementioned inflation–based limits.
  - o There is a volume adjustment included in price controls, to compensate *Royal Mail* for fixed–costs related to network management.
  - o Price controls also include a component to raise prices if *Royal Mail’s* pension deficit rises.
  - o Finally, prices are required to be reduced if *Royal Mail* does not meet its quality–of–service targets.

- Greater cost transparency and accounting separation
  - o Costing methodology must be improved in order to (i) introduce guiding principles to define the fundamental requirements for *Royal Mail’s* cost reporting to be suitable for regulatory reporting purposes; (ii) introduce methodological principles to define the basic rules and concepts and specific methodology for such reporting; (iii) introduce a detailed costing manual for internal purposes, with any changes reported to Postcomm in advance.
  - o Accounting separation must be further implemented and adapted in order to perfectly reflect the difference between regulated products and non–regulated products, upstream and downstream operations, and bulk and non–bulk products.
  - o The accounts must also better show true costs and inputs, and must continue in the direction of their reconciliation with audited statutory accounts.
  - o Accounts must also be independently audited for their conformity with a regulatory accounting framework.

- Modifications to *Royal Mail’s* universal service provider license<sup>[2]</sup>
  - o *Royal Mail’s* license must be clarified and modified to reflect changing circumstances and legislative changes.
  - o The compliance officer attributed to *Royal Mail* will be assigned an expanded role, in order to oversee compliance with all provisions of the license, rather than simply oversee that full and complete information is provided to Postcomm (according to conditions 6 and 7 of *Royal Mail’s* license)

This new framework is intended to be progressively implemented over the coming years, with

partial implementation by April 2011 and full implementation achieved by April 2012.

*PS:* The main document is 80 pages long, and is followed by five annexes (1. Provision of a universal service ; 2. Analysis of Markets; 3. Cost transparency and accounting separation; 4. Price control and access; 5. Licensing Review).

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[1] Priority mail is supposed to be delivered the day following posting; economy mail is supposed to be delivered two or more days following posting.

[2] Full-text License available at

[ftp://ftp.royalmail.com/Downloads/public/ctf/rmg/Royal\\_Mail\\_Licence\\_25%20May\\_\\_2006.pdf](ftp://ftp.royalmail.com/Downloads/public/ctf/rmg/Royal_Mail_Licence_25%20May__2006.pdf)

### **Links with other documents in the same sector**

Cf. Regulatory Law Review, 2010, III.2-6 and III.2-3. The first report concerns a report commissioned by the ARCEP (the French postal and telecommunications regulator) from an independent consulting firm on intangible benefits to La Poste (the French postal service) from its universal service obligations.

The second report concerns a document published by the United States Postal Service on the challenges it faces in continuing to fulfill its universal service obligations under the current regulatory environment.

### **BRIEF COMMENTARY**

This document is primarily interesting for the philosophical stance it takes on regulation of the postal sector.

Indeed, sector-specific regulation is needed in the postal sector in order to implement asymmetrical regulation that allows new entrants to compete with the historical monopolist, and to prevent the market-dominant firm from evincing weak competitors with its strength.

Sector-specific regulation is also needed to ensure that the universal service provider effectively fulfils its universal service obligations, without depriving it of a level of revenue that ensures either profitability or minimal reliance on public subsidies. In this sense, it is a permanent regulatory framework. Postcomm, without eschewing such sector-specific regulation, has announced its intention in this document to reduce such regulation to the minimum level required to accomplish these goals, leaving to general Competition Law (administered by the Office of Fair Trading) oversight of sectors in which competition has adequately taken root. We find in this way the general conception of Regulation in the United Kingdom, where Competition Law is preferred, whenever possible, to Regulatory Law, and where Regulatory Law is often simply a means for moving a sector towards general Competition Law. This is opposed to the French or North American general theory of Regulation, where we do not encounter such a liberal conception of the meaning of Regulation.

In conclusion, we believe that this goal is both laudable and delicate: it is laudable because sector-specific regulation is by nature transitory and teleological, but it is at the same time delicate because abandoning sector-specific regulation before competition has fully taken root in the sector contains the risk of erasing all progress made by Postcomm's regulation of this sector up to this point.