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5<sup>th</sup> January 2012

Dear Gavin,

**SECURING THE UNIVERSAL SERVICE: PROPOSALS FOR THE FUTURE  
FRAMEWORK FOR ECONOMIC REGULATION**

1.1 MUA would like to thank the Regulator for the opportunity to respond to its Securing the Universal Postal Service consultation. As you will be aware, a selection of MUA members have attended the various workshops and working groups set up to discuss these proposals, and a sub group has subsequently met to discuss them in more detail. Following a brief introductory section, the points made below therefore represent the culmination of membership discussion on the matter, and is MUA's generally held view, albeit that there may be certain sectors of membership with slightly varying views on certain points, which will be represented in more detail in their own submissions.

**Mail Users' Association**

1.2 MUA is Britain's only independent association of business users wholly concerned with commercially related postal matters. Its members are drawn from a wide range of business interests including direct mail, banking and finance, communications and utilities, publishing and postal related industries.

1.3 Collectively, it is estimated MUA members generate more than 20% of annual postal traffic in the UK. MUA's primary objective is to secure a healthy and cost effective range of postal services for all business users and their customers. This not only applies to physical mail, but also includes electronic and hybrid mail areas.

1.4 MUA believes that this can be achieved in a mixed competitive market, offering users a real choice between the services of Royal Mail and a set of competing value added options from other carriers - particularly for the business mailer.



1.5 In order to achieve this goal, MUA believes it is necessary to ensure service providers are:

- customer focused in their approach to the products and services they offer;
- are able to offer cost effective services at realistic prices the market can bear;
- have flexibility in their approach to customers whose needs are continually changing; and,
- are able to provide reliable, high quality services on a continual basis.

## **2. Key Concerns with the Proposals**

2.1 MUA acknowledges the reasoning set out in Ofcom's consultation document regarding the future regulation of UK postal services in the present circumstances. However, as has been stated by members at meetings with the Regulator, MUA continues to have strong reservations about the potential implications of adopting such a light touch regulatory regime. In the Industry's experience, Royal Mail has historically relied upon revenue generating pricing strategies rather than addressing the more challenging aspects of modernisation, and given the financial position in which the national carrier now finds itself, members have strong concerns about the likely outcome of this new regulatory approach, and the consequential impact further price increases would have on a postal market already under considerable pressure from electronic substitutes.

2.2 MUA would contest arguments apparently suggested by Royal Mail that mail volume decline as a result of the last price increases was over estimated by Industry, and that as a result, bulk mail pricing elasticity is arguably greater than anticipated. On the contrary, members believe changes in customer behaviour (and more specifically initiatives ultimately designed to migrate traditional mailers towards e-substitution as a result of those price increases) has yet to hit the market, and would argue a 'lag effect' caused by complex decision making processes and budgetary planning within large organisations has actually delayed the expected impact.

2.3 Indeed, a qualitative feedback consultation carried out amongst large mailing organisations in MUA membership indicates that the last price increase drove postal spend onto the Boardroom agenda, and triggered a large amount of activity within such organisations, including planned reductions in marketing spend/ mailing volumes, the movement of mailing activity back in-house, and initiatives to put in place mandatory mailing by e-alternatives, all of which given the afore mentioned lag effect are unlikely to impact on the market until 2012-13<sup>1</sup>.

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<sup>1</sup> Please also see Postcomm Business Customer Survey Summary 2009 - Page 6-7



2.4 In light of this, MUA has strong concerns that if postal prices are allowed to be ratcheted up over the next 2-3 years, a tipping point will be reached (possibly in 4-6 years), after which time the postal sector will enter new territory as companies are compelled to impose 'opt ins'/charging for paper statements, the expansion of e-billing operations, the introduction of mandatory e-substitution strategies within organisations, and the reversion of organisations to the stamp payment channel (a loss making part of Royal Mail's business). The concern being that when this tipping point is reached mail volumes on which the sustainability of the USO ultimately relies will be lost for good, resulting in the UK postal market falling into an inescapable spiral of decline. MUA therefore considers there is a case for Ofcom putting in place some sort of control over a given time span to protect against rapid price increases followed by rapid volume decline, thereby tying in the time lag for change in inelastic mail volumes.

2.5 This foreseeable position could potentially be compounded further, by the fact that there is increasing concern Royal Mail retail products could also become subject to VAT as a result of them being removed from the Universal Service – a situation that would have a devastating effect on financial services, charities and public sector organisations unable to recover it, all of whom provide a significant contribution to the daily mailbag. Whilst MUA recognises decisions surrounding the imposition of VAT on post are a matter for HMRC, members believe Ofcom has to take into account when fulfilling its primary duty of protecting the USO, the considerable effect the imposition of VAT would have on these sectors of the business, and the knock on effect it would have on the universal service.

2.6 MUA would therefore urge Ofcom to factor into any future price control, contingency arrangements to mitigate the effects of a potential 'double whammy' price increase. And as part of this work, would strongly urge Ofcom to establish from HMRC what the outcome is likely to be, and provide for contingency given the potential impact such a move would have on these key mail volume contributors.

### **3. Further Observations on the Proposals**

3.1 In addition to these primary concerns, MUA would wish to make a number of other points:

- **Regulatory Time Frame** – MUA is concerned that the seven year timeframe proposed by Ofcom is too long, and that at the very least there should be an interim review midway through the period to re-assess the affordability of mail and the impact of any aforementioned lag effect.



- **Regulatory Safeguards - Profitability of the USO** – MUA would wish to see a financial breakdown of the split between stamp and business mail contributions to the USO, in order to understand any claims made in future by Royal Mail concerning the profitability/loss in these component parts, by way of substantiating its case for future price increases in any given area.
- **Regulatory Safeguards – Price Caps** – MUA is generally of the view that there should be a price cap applied to both 1<sup>st</sup> and 2<sup>nd</sup> Class stamps (all weights). Members consider this safeguard is important in order to protect against the national carrier raising the prices of 1<sup>st</sup> Class products to such an extent that down-trading to 2<sup>nd</sup> Class reaches the point where Royal Mail could arguably make the case for its removal from the USO on financial grounds. Members do not believe this would be in the interests of the UK postal industry and believe Ofcom needs to re-consider the business consequences of 1<sup>st</sup> Class prices escalating to a point where social and SME customers are forced to switch to 2<sup>nd</sup> Class products purely on pricing grounds.
- **Efficiency Improvements** – MUA would note Ofcom has not yet indicated the year-on-year levels of efficiency gains it would deem appropriate for Royal Mail to achieve when modernising the business, and members would state that they are not convinced Royal Mail is ultimately in a position to strip costs out of the business, and/or make efficiency gains at anything like a commercially acceptable speed.
- **Dispute Resolution** – MUA believes Ofcom should put a published dispute resolution procedure in place, and that in circumstances where there is sufficient weight of evidence in favour of regulatory intervention, the Regulator should be prepared to take the case forward. Members are extremely concerned that under Ofcom's proposed regulatory framework Royal Mail could potentially impose unfair and unreasonable terms and conditions on business mailers, and that at present there is no mechanism in place in the proposals to challenge such changes on a national level. Historical examples of such unreasonable changes can be found in Royal Mail's Retail Zonal Pricing application (eventually quashed by Postcomm as being unreasonable to customers), and more recently in what many believe is Royal Mail's unfair approach to 'Reversions' for mailings failing to meet specifications that many would argue are redundant and impractical.
- **Definition of Vulnerable Customers** – MUA would argue Ofcom's definition of what constitutes 'vulnerable customers' is insufficiently broad. Given that Royal Mail is to all intents and purposes a monopoly, the reliance of many SME's on the national carrier must also define them as being vulnerable customers, and as such this sector of the market should be taken into account in any consequent safeguards relating to them.



- **Monitoring of Royal Mail's Performance** – As an independent regulator, MUA would expect Ofcom to gain all the necessary information with which to regulate the business. Industry does not have a full picture of Royal Mail's business plan, therefore members consider Ofcom is best placed to decide which areas need to be monitored in order to ensure Royal Mail achieves appropriate targets and efficiency gains. Members would note however that the vast majority of organisations benchmark their activities against competitors, and in a similar vein would expect Ofcom to have efficiency testing measures in place to compare Royal Mail's efficiency against other European counterparts. Members would also suggest Ofcom needs to provide the industry with a published statement of the information it intends to collect/monitor, and wherever possible provide a financial breakdown of information relating to the profitability of the USO, in order to allow key stakeholders to understand the decisions being taken in relation to it.
- **Inaccurate Mail Volume Predictions** – MUA believes Ofcom should put in place a review mechanism that would be triggered were mail volumes to vary considerably from those predicted, thereby enabling a timely re-evaluation of changing market circumstances.
- **Assessment of E-to-E Competition/Notification Condition** – Whilst MUA recognises Ofcom is obliged by the Secretary of State to put in place an assessment process for incoming end-to-end competition, members are nevertheless concerned this may deter potential competitors from market entry, and thereby arrest customer choice in the end-to-end delivery arena.

3.2 Finally, I would also like to highlight ahead of time an area of concern for members in Ofcom's Review of Regulatory Conditions consultation, this being the removal of the notice period historically provided to business customers for changes to bulk mail prices and terms and conditions. This is an issue that MUA would wish to discuss in more detail, and given the short consultation timeframe I would like to invite Ofcom representatives to attend MUA's Inland Committee held on the morning of 13 January to discuss this matter.

3.3 I hope that you find this information useful in your deliberations. Should you wish to discuss anything that may assist further, do not hesitate to give me a call.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Alan MJ Halfacre". The signature is fluid and cursive, with a large loop at the end.

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