



# Review of Regulatory Conditions

Postal Regulation

Consultation

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## Section 1

# Executive summary

## The context and scope of this consultation

- 1.1 Under the Postal Services Act 2011 ('the Act') Ofcom took over responsibility for regulating the postal sector on 1 October 2011. Our primary duty under the Act is to carry out our functions in relation to post in a way which we consider will secure the provision of a universal postal service.
- 1.2 Amongst other things, the Act also required Ofcom to transpose the existing licences into regulatory conditions under a general authorisation regime. The first regulatory conditions took effect from 1 October 2011<sup>1</sup> and have substantially the same effect as the conditions in the old licences.
- 1.3 On 20 October 2011 we published our consultation *Securing the Universal Postal Service: Proposals for the future framework for economic regulation* ('the October consultation')<sup>2</sup>. In this document we set out proposals that supported our view that the best approach to fulfilling our primary duty was to allow Royal Mail far greater commercial freedom with regard to setting prices. We also said:
- “in a competitive market it is important that there is also sufficient flexibility to allow Royal Mail, as well as its competitors, to innovate; to improve existing services or introduce new services that are beneficial to its customers and users. The previous licence-based regime set constraints on Royal Mail, in terms of having to publicly notify the market of its intentions and to obtain regulatory agreement to changes in its regulated products.
- “While such a regime provides stability and clarity for customers, users and the market, it can represent a significant reduction in commercial freedom for Royal Mail in responding to a challenging market environment. We intend to consider this issue further and will be presenting proposals later in the year as part of a wider review of regulatory conditions, but our intention will be to simplify the obligations and wherever appropriate to consider the benefits of permitting greater commercial freedom for Royal Mail<sup>3</sup>”.
- 1.4 In line with this approach, we are now consulting on a number of wide-ranging changes to the regulatory conditions to ensure that they remain fit for purpose and are consistent with our wider objectives (to simplify the regulatory regime and provide

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<sup>1</sup> Ofcom *Postal regulation: Transition to the new regulatory framework*, 29 September 2011, <http://stakeholders.ofcom.org.uk/binaries/consultations/postal-regulation/statement/statement.pdf> .

<sup>2</sup> Ofcom *Securing the Universal Service: Proposals for the future framework for economic regulation*, 20 October 2011, <http://stakeholders.ofcom.org.uk/binaries/consultations/securing-the-postal-service/summary/condoc.pdf> .

<sup>3</sup> Paragraphs 1.65 – 1.66 of the October consultation.

greater commercial flexibility to Royal Mail whilst still ensuring that we secure the universal postal service)<sup>4</sup>.

- 1.5 In this document, we set out a draft universal service postal order and propose changes to the designated universal service provider ('DUSP') conditions which apply to Royal Mail<sup>5</sup>. We also propose to change other regulatory requirements, including the consumer protection conditions which apply to postal operators and/or Royal Mail.
- 1.6 In addition, this review contains draft legal instruments showing how we would go about implementing the proposals we made in our October consultation regarding the safeguard cap for Second Class stamps, access and regulatory accounting, subject to responses to that consultation<sup>6</sup>.

## Proposals

- 1.7 While we propose changes to the vast majority of the existing conditions, many of these are either fairly minor or they implement the approach already proposed to stakeholders in our October consultation.
- 1.8 There are three key areas where we make new proposals. These relate to:
- a) The first universal postal service order ('UPSO' or 'order')<sup>7</sup> and adjustments to DUSP conditions;
  - b) The publication and advance notification requirements for the price and non-price terms of Royal Mail's services; and
  - c) A new condition which would require postal operators to notify us of their plans to provide (or expand) an end-to-end letters delivery service.

### The first universal postal service order and related DUSP conditions

- 1.9 The universal postal service is currently set out in DUSP condition 1, which has substantially the same effect as the equivalent in Royal Mail's former licence. However, under s30 of the Act, we have to make an 'order' which sets out a *description* of the services that should be provided as a universal service, as well as the standards with which those services are to comply.
- 1.10 We therefore make proposals to describe the characteristics of universal service products via an order and consequential revisions to DUSPs. This will clarify the product characteristics for customers and ensure that services which meet these characteristics are provided by Royal Mail.

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<sup>4</sup> We stated we would do this review in the update to our Annual Plan: Ofcom *Supplement to Annual Plan 2011/12 – regulation of postal services*, 8 August 2011, [http://www.ofcom.org.uk/about/annual-reports-and-plans/annual-plans/files/2011/08/Postal\\_Services\\_Annual\\_Plan.pdf](http://www.ofcom.org.uk/about/annual-reports-and-plans/annual-plans/files/2011/08/Postal_Services_Annual_Plan.pdf).

<sup>5</sup> Royal Mail is the UK's designated universal postal service provider ('USP').

<sup>6</sup> Given the close linkages, we will take account of the conclusions to the October consultation when completing our review of the regulatory conditions.

<sup>7</sup> An order under s.30 of the Act is a type of statutory instrument. Under s.63 of the Act and s.403 of the Communications Act, we must consult before making it but it is not laid before Parliament.

- 1.11 However, we do not propose any substantive change to the universal service at this stage.
- 1.12 This consultation is an opportunity for us to test our proposals, as this is the first time that the universal service will have been described in this way. Currently, the obligation on Royal Mail to provide the universal service is set out mainly by a list of names of products. Arguably, there could therefore be some debate about the characteristics of the products, and the terms and conditions which should be part of the product definition. As we move away from the current system, we ask for feedback on whether we have captured the essential features of the current service, or if we should add, remove or modify some of the characteristics we propose.

### **Notification and publication requirements for the price and non-price terms of Royal Mail's services**

- 1.13 The previous licence-based regime required Royal Mail to publish its price and non-price terms for universal and non-universal services three months in advance of any change coming into effect. In addition, Royal Mail required regulatory agreement to make non-beneficial changes to its regulated services<sup>8</sup>. As set out in the October consultation, we consider it is important to give more flexibility and commercial freedom to Royal Mail so it can respond to a challenging market environment and innovate, which may, in turn, allow it to improve existing services (or introduce new ones) which are beneficial to its customers.
- 1.14 We continue to believe that residential and/or business customers will require some notice of changes to the price and non-price terms for universal services. But we propose that the requirement on Royal Mail can be reduced from the current three months to a minimum one month advance notice period for changes to its universal services. Royal Mail will be free to give longer notice to customers if they consider it necessary.
- 1.15 In addition, we propose not to require Royal Mail to publish prices and terms and conditions or give advance notice of changes for retail non-universal services because most non-universal service customers have a choice of operator. We therefore consider that Royal Mail would be incentivised to provide sufficient notice to its retail non-universal service customers in the absence of a regulatory requirement.
- 1.16 We are also proposing that Royal Mail should not have to obtain regulatory approval for any changes it wishes to make to universal services. However, we are proposing that the terms and conditions for universal services should be fair and reasonable and we would reserve the right to intervene if we did not believe that was the case. Furthermore, as we intend to describe the characteristics which Royal Mail's universal services must have (which in practical terms means retaining core features of its current universal service products), this should provide protection for consumers and reduce the potential impact from any changes Royal Mail may make to subsidiary product features (not defined as characteristics).

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<sup>8</sup> This requirement refers to the terms and conditions on which the regulated services were offered and provided in March 2006. In practice Royal Mail has applied this requirement to any non-price change that is mandatory for customers to implement.

## **New notification condition for end-to-end entry (or expansion)**

- 1.17 We also present a proposal for a new (notification) condition<sup>9</sup> which would require any postal operator which seeks to introduce or expand a competing letters delivery service (above particular thresholds<sup>10</sup>) to notify us at least three months in advance so we can assess the impact of its plans on universal service provision.

## **Other proposals**

- 1.18 Our transitional regulatory regime also included five transitory conditions which took effect on 1 October 2011. These will cease to apply when the first universal service order comes into force, which we intend to be 1 April 2012. A transitory condition is one which includes obligations which we would not have the power to impose under Part 3 of the Act. Some of the previous licence conditions were transposed as transitory conditions because they contained a mixture of obligations (i) some of which we would not have the power to impose under Part 3 of the Act, but also (ii) some of which we would have the power to impose.
- 1.19 We have considered whether there is a case for retaining any of the obligations which we would have the power to impose, beyond the date that they would otherwise cease to have effect. Our proposal in this regard is not to retain any such obligations and they would therefore cease to have effect in their entirety from April 2012, as planned.
- 1.20 Finally, our proposals in this review show how we would go about implementing the safeguards set out in our October consultation. We set out proposed drafting for a Second Class stamp price cap – the safeguard for vulnerable customers<sup>11</sup>.
- 1.21 We also propose a new access condition for Royal Mail which would implement our earlier proposals on access requirements. The condition would require Royal Mail to provide access on fair and reasonable terms, and to maintain a margin between its access prices and its equivalent retail services. We have also included supplementary proposals on the approach to regulating the terms and conditions of access, including the extent to which the condition should specify minimum requirements which Royal Mail should include within the access framework.
- 1.22 Finally, we present a regulatory accounting condition in order to implement our earlier proposal for Royal Mail to maintain appropriate accounting and financial records. This condition aims at providing a higher level of transparency which is necessary for our proposed monitoring regime.

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<sup>9</sup>In October this year, the Secretary of State directed us to impose a notification condition – see <http://www.bis.gov.uk/policies/business-sectors/postal-services/postal-services-acts> – under s.41 of the Act and we have until 1 April 2012 to put this in place.

<sup>10</sup>A notification would be required if the operator was - in the quarter following the notification period - (a) planning to enter the market and deliver more than 2.5M letters anywhere in the UK or (b) to increase the volume of letters they were carrying by more than 2.5M.

<sup>11</sup> This cap is subject to responses to our ongoing consultation on the policy and may change depending on responses to that consultation.

## Next steps

- 1.23 Following consideration of responses, we plan to issue our statement before 1 April 2012 to coincide with the new financial year and to ensure consistency with related changes from our wider work on postal regulation.
- 1.24 This document has a six week consultation period which we have extended by an additional week given the public holidays towards the end of this month. Interested parties are therefore requested to submit responses to this consultation to us by 31 January 2012.



## Section 2

# Introduction

## Introduction

- 2.1 The framework for our assessment of any regulatory safeguards in relation to Royal Mail's pricing of postal services is set out in the Act<sup>12</sup>, which received Royal Assent on 13 June 2011. One of the Act's main purposes is to make provision for a new regulatory framework for the postal services sector, including transferring regulatory responsibility from Postcomm to Ofcom. The vesting of this new responsibility for Ofcom took place on 1 October 2011.
- 2.2 This framework is set out in Part 3 of the Act, which came into force on 1 October 2011. Its provisions also give effect to Directive 2008/6/EC of the European Parliament and of the Council of 20 February 2008, which amends Directive 97/67/EC with regard to the full accomplishment of the internal market of Community postal services.
- 2.3 The Act also replaced the existing licensing regime in the postal sector with a general authorisation regime. This means that persons may provide postal services without the need for any licence or authorisation but that the provision of those services by postal operators may be subject to regulatory conditions that Ofcom may impose under Part 3 of the Act<sup>13</sup>.
- 2.4 The rest of this Section summarises the key features of the legal framework which are relevant to the proposals set out in this consultation.
- 2.5 The purpose of this consultation is to seek input from stakeholders and any other interested parties. In particular, whilst this consultation document contains a number of specific questions, we are not seeking to limit the issues on which respondents may wish to comment, and respondents are invited to include representations on any issues which they consider to be relevant.

## Duty to secure provision of a universal postal service

- 2.6 Section 29(1) of the Act provides that Ofcom must carry out its functions in relation to postal services in a way that it considers will secure the provision of a universal postal service. Section 29(2) of the Act provides that Ofcom's power to impose access or other regulatory conditions is subject to the duty imposed by section 29(1) of the Act.
- 2.7 The universal postal service must, as a minimum, include each of the services in section 31 of the Act - these are set out in Section 4 of this document.
- 2.8 Section 29(3) of the Act provides that, in performing our duty under section 29(1), we must have regard to the need for the provision of a universal postal service to be:
  - financially sustainable; and

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<sup>12</sup> <http://www.legislation.gov.uk/ukpga/2011/5/contents/enacted>

<sup>13</sup> The types of conditions we can impose are those in sections 36, 38, 39, 41, 42, 48-51 of the Act.

- efficient before the end of a reasonable period and for its provision to continue to be efficient at all subsequent times.

2.9 Section 29(4) of the Act states that ‘financially sustainable’ includes the need for a reasonable commercial rate of return for any universal service provider on any expenditure incurred by it for the purpose of, or in connection with, the provision by it of a universal postal service.

### **The duty to secure the provision of sufficient access points**

2.10 Section 29(6) of the Act provides that Ofcom’s duty under section 29(1) includes a duty to carry out its functions in relation to postal services in a way that Ofcom considers will secure the provision of sufficient access points to meet the reasonable needs of users of the universal postal service. This duty is subject to any direction by the Secretary of State for Ofcom to take, or refrain from taking, specified action. No such direction has to date been given to Ofcom.

2.11 The term ‘access point’ is defined at section 29(11) of the Act as meaning any box, receptacle or other facility provided for the purpose of receiving postal packets, or any class of postal packets, for onwards transmission by post.

### **General duties**

2.12 Section 3 of the Communications Act 2003 (the “2003 Act”) provides that it shall be our principal duty, in carrying out our functions, to further the interests of citizens in relation to communications matters and to further the interests of consumers in relevant markets, where appropriate by promoting competition.

2.13 This principal duty applies also to functions carried out by us in relation to postal services. Section 3(6A) of the 2003 Act provides that the duty in section 29(1) of the Act takes priority over our general duties in the 2003 Act in the case of conflict between the two where we are carrying out our functions in relation to postal services.

2.14 In performing our general duties, we are also required under section 3(4) of the 2003 Act to have regard to a range of other considerations, which appear to us to be relevant in the circumstances. In this context, we consider that a number of such considerations appear potentially relevant, including:

- the desirability of promoting competition in relevant markets;
- the desirability of encouraging investment and innovation in relevant markets;
- the vulnerability of children and of others whose circumstances appear to Ofcom to put them in need of special protection;
- the needs of persons with disabilities, of the elderly and of those on low incomes;
- the opinions of consumers in relevant markets and of members of the public generally;
- the different interests of persons in the different parts of the United Kingdom, of the different ethnic communities within the United Kingdom and of persons living in rural and in urban areas;

- the extent to which, in the circumstances of the case, the furthering or securing of the matters mentioned in section 3(1) is reasonably practicable.
- 2.15 Section 3(5) of the 2003 Act provides that in performing our duty to further the interests of consumers, we must have regard, in particular, to the interests of those consumers in respect of choice, price, quality of service and value for money.
- 2.16 Pursuant to section 3(3) of the 2003 Act, in performing our general duties, we must have regard, in all cases, to the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed, and any other principles appearing to us to represent the best regulatory practice.
- 2.17 In this regard, we note Ofcom's general regulatory principles<sup>14</sup> including in particular the following in the present context:
- ensuring that our interventions are evidence-based, proportionate, consistent, accountable and transparent in both deliberation and outcome;
  - seeking the least intrusive regulatory mechanisms to achieve our policy objectives;
  - consulting widely with all relevant stakeholders and assessing the impact of regulatory action before imposing regulation upon a market.
- 2.18 Finally, we have an ongoing duty under section 6 of the 2003 Act to keep the carrying out of our functions under review with a view to ensuring that regulation by Ofcom does not involve the imposition of burdens which are unnecessary or the maintenance of burdens which have become unnecessary.
- 2.19 Ofcom can potentially impose eight types of condition on different types of postal operator:
- A designated USP condition;
  - A USP access condition;
  - A USP accounting condition;
  - A general universal service condition;
  - A notification condition;
  - An essential condition;
  - A general access condition; and
  - A consumer protection condition.

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<sup>14</sup> See this link for a full list of the principles, <http://www.ofcom.org.uk/about/what-is-ofcom/statutory-duties-and-regulatory-principles/> .

## The initial conditions

- 2.20 Under the transitional provisions set out in the Act<sup>15</sup> we were, in effect, required to transpose the existing regulatory conditions which were contained in postal operators' licences into conditions under a general authorisation regime and to apply these from 1 October 2011. For the transitional period, these conditions ('the initial conditions') had to be substantially similar to the conditions previously contained in licences, except where we considered that a condition was no longer necessary<sup>16</sup>.
- 2.21 On 29 September 2011, we issued our statement on the transitional regulatory regime<sup>1</sup>. This included our transposition of the existing postal licence conditions into initial conditions to apply under the general authorisation regime as well as our provisional designation of Royal Mail as the universal service provider.
- 2.22 This regime took effect from 1 October 2011 and consisted of the following conditions:
- One essential condition ('E1') which applied to regulated postal operators ('RPOs') and nine consumer protection (CP 1-9) conditions whose requirements vary in terms of their coverage, applying either to all postal operators, all RPOs or just to Royal Mail;
  - Eleven conditions which apply to Royal Mail as the USP – six designated USP conditions ('DUSP 1-6'), four access conditions ('USPA 1-4') and one accounting condition ('ACC 1'); and
  - Five transitory (i.e. time-limited) conditions – four on the universal service provider ('T 1-4') and one on RPOs ('T 5').
- 2.23 In this document, we set out how we have considered whether these conditions need to be amended, deleted or whether new conditions should be introduced. The next Section also explains in more detail our overall approach to this review.

## General test for imposing or modifying regulatory conditions

- 2.24 Schedule 6 to the Act<sup>17</sup> provides that we may impose or modify a regulatory condition only if we are satisfied that the condition or modification:
- is objectively justifiable;
  - does not discriminate unduly against particular persons or a particular description of persons;
  - is proportionate to what it is intended to achieve; and
  - is transparent in relation to what it is intended to achieve.

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<sup>15</sup>Under Part 3 and Schedule 9 of the Act.

<sup>16</sup>Apart from consumer protection conditions.

<sup>17</sup>The expression 'regulatory condition' is defined in section 28(2) of the Act as including a designated USP condition and a USP access condition; that definition applies to Schedule 6 by virtue of sections 53 and 63 of the Act, when read together.

- 2.25 Individual regulatory conditions provided for in the Act go on to set out specific tests which we must be satisfied are met before they can be imposed.
- 2.26 We consider each of these tests at the end of each Section in this document where we make proposals to change existing conditions or add a new one.

## General impact assessment

- 2.27 The analysis presented in the whole of this document represents an impact assessment, as defined in section 7 of the 2003 Act.
- 2.28 Impact assessments provide a valuable way of assessing different options for regulation and showing why the preferred option was chosen. They form part of best practice policy-making. This is reflected in section 7 of the 2003 Act, which means that generally Ofcom has to carry out impact assessments where its proposals would be likely to have a significant effect on businesses or the general public, or when there is a major change in Ofcom's activities. However, as a matter of policy Ofcom is committed to carrying out and publishing impact assessments in relation to the great majority of its policy decisions. For further information about Ofcom's approach to impact assessments, see our guidelines<sup>18</sup>.
- 2.29 Specifically, pursuant to section 7, an impact assessment must set out how, in our opinion, the performance of our general duties (within the meaning of section 3 of the Act) is secured or furthered by, in relation to what we propose.

## Regulatory impact assessment for the proposed universal service order

- 2.30 The regulatory impact assessment for our proposed universal service order is provided separately, at Annex 7. This is because it is Ofcom's practice to prepare and lodge in the Parliamentary library regulatory impact assessments for legislation even when not laid before Parliament.

## Equality impact assessment

- 2.31 In carrying out our functions, we are also under a general duty under the Equality Act 2010 to have due regard to the need to:
- eliminate unlawful discrimination, harassment and victimisation;
  - advance equality of opportunity between different groups; and
  - foster good relations between different groups,
- in relation to the following protected characteristics: age; disability; gender re-assignment; pregnancy and maternity; race; religion or belief; sex and sexual orientation.
- 2.32 Such equality impact assessments ("EIAs") also assist us in making sure that we are meeting our principal duty under section 3 of the 2003 Act discussed above.

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<sup>18</sup>*Better Policy Making – Ofcom's approach to Impact Assessment*, Ofcom, 21 July 2005  
[http://stakeholders.ofcom.org.uk/binaries/consultations/better-policy-making/Better\\_Policy\\_Making.pdf](http://stakeholders.ofcom.org.uk/binaries/consultations/better-policy-making/Better_Policy_Making.pdf)

- 2.33 We have therefore considered what (if any) impact the proposals in this consultation may have on equality. We do not consider the impact of the proposals in this consultation to impact on any particular group within society.
- 2.34 We have therefore not carried out separate EIAs in relation to race or gender equality, or equality schemes under the Northern Ireland and Disability Equality Schemes.

## Section 3

# Our approach to this review

## Scope and timing of this consultation

- 3.1 We committed to a review of the regulatory conditions in our update to the annual plan. We said we would consult by December on changes that would ensure those conditions remained fit for purpose and to bring changes into effect by the start of April.
- 3.2 Our review is wide-ranging in scope, covering the following areas:
- amending the regulatory conditions in line with a general authorisation-type regime and simplifying them where appropriate (to remove unnecessary restrictions on postal operators);
  - proposing the first UPSO and related changes to DUSP conditions as a result of the move to describe the universal service rather than listing the products of which it is composed;
  - proposing knock-on changes to conditions to show how we would go about implementing the proposals we made in the October consultation such as the Second Class stamp safeguard cap; the access requirements; and the revised approach to accounting and financial reporting – all subject to responses to that consultation;
  - the advance notification and publication requirements for the price and non-price terms of Royal Mail's services;
  - ensuring Royal Mail's performance targets are maintained for universal services to avoid the risk of quality of service being reduced;
  - setting out a proposed notification condition on other postal operators for potential end-to-end entry or growth into a (competing) letters delivery service; and
  - considering whether to retain any aspects of the five transitory conditions, which are due to expire at the end of March 2012.
- 3.3 We note that we intend to undertake a further review of the needs of postal users – by April 2013 – which will inform our work on universal services over the longer term. This is required by s.30 of the Act, which states that we must carry out an assessment of the extent to which the postal services market meets the reasonable needs of postal users, before any changes to the universal postal service order can be made.

## Changes which reflect and fit with wider work on postal regulation

- 3.4 We are proposing changes to most of the conditions. The existing conditions reflect the previous licensed based approach as we were required to transpose them ensuring they were to “substantially the same effect”.

- 3.5 The requirements now need to be considered in light of the need to ensure the viability of the universal service which was explained in our October consultation (e.g. the trend for falling letter volumes and revenues). They also need to take account of the competition which now exists in non-universal postal services such as bulk mail.
- 3.6 We consider that the changes we propose should help to give operators commercial flexibility by removing unnecessary regulation, where appropriate, while at the same time, focusing the regulatory regime so that it helps to secure the universal service (which includes the use of safeguards, such as appropriate monitoring mechanisms).
- 3.7 There is a strong linkage between this review and the October consultation – as this review includes proposals to implement some of the proposed policy set out in the latter document. Clearly we will take account of the conclusions to the October consultation when completing our statement on regulatory conditions. We also expect that the statements for both documents could be issued around the same time and this would provide clarity on the overall regulatory framework to stakeholders.

## The conditions reviewed and the potential impacts of our proposals

- 3.8 We have reviewed all existing 21 conditions plus the five transitory conditions, considering whether any requirements in these conditions should be left unchanged, amended or deleted (and whether we should merge conditions in order to simplify the regulatory regime).
- 3.9 We have also considered whether we need to impose any additional conditions.
- 3.10 We set out numerous proposals to change the regulatory conditions that we put in place when we transposed the previous licence conditions. While in some cases, there is no change to the condition or no material alteration to the nature of the existing obligations, in other cases, we do propose either minor changes (such as corrections) or more significantly a revised approach to condition requirements.
- 3.11 We have been directed by the Secretary of State to put in place an additional 'notification' condition for potential end-to-end entry or expansion. Therefore, in this document we set out our proposals in relation to this condition.
- 3.12 In the remaining sections of this document, there is discussion of any potential impacts arising from our proposals and this will form our impact assessment (IA).
- 3.13 However, we do not discuss impacts in any detail for proposals already set out and discussed in our October consultation i.e. in relation to the safeguard cap for vulnerable customers on Second Class stamps, to access requirements and also the new accounting and financial reporting approach. That is because, in this review, we are essentially explaining how we would implement those earlier proposals via consequential changes to the regulatory conditions. If stakeholders have views on the substantive policy proposals contained in the October consultation we encourage them to respond to the earlier consultation (its closing date for responses is 5 January 2012).

## Outline of the rest of this document

- 3.14 The rest of this document is laid out as follows:
- **Section 4** sets out our proposals for the first Universal Postal Service Order;



- **Section 5** presents our proposed approach for the DUSP conditions which relate to the provision of the universal postal service, including the performance standards of those services as well as the provision of information to users on the price and non-price terms for universal services (we also discuss our approach to advance notification and publication requirements for the price and non-price terms of *non*-universal services; and *non*-universal service standards within this Section);
- **Section 6** presents our proposals for consumer protection conditions, and discusses the one essential condition (on mail integrity);
- **Section 7** presents a proposed additional condition to cover requirements for the end to end notification process;
- **Section 8** sets out our proposal to implement the safeguard cap for Second Class stamps;
- **Section 9** sets out our proposal to implement access requirements via a singular access condition;
- **Section 10** presents our proposed implementation of regulatory accounting requirements;
- **Section 11** sets out our proposals for handling the cessation of the transitory conditions;
- **Annex 5** sets out the conditions we propose and how they relate to those under the previous licence regime and the current initial conditions;
- **Annex 6** illustrates the characteristics of universal services that we propose to specify in regulation;
- **Annex 7** is our regulatory impact assessment for the first UPSO;
- **Annex 8** provides an appendix on regulatory accounting; and
- **Annexes 9 to 17 - which are published separately on our website<sup>19</sup>** - contain the draft text of the first universal postal service order as well as our draft notifications on DUSP conditions; the consumer protection conditions; the essential condition; the USP access condition; the USP regulatory accounting condition (and also its related direction); the end to end notification condition; and finally, the notification to revoke and amend the regulatory conditions imposed on 1 October 2011.

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<sup>19</sup> Given the degree of change we are proposing to make in our draft conditions, we have in most cases not highlighted (in colour) the text being changed nor tracked our changes to the existing conditions. If stakeholders wish to view the text of the existing conditions, for comparison, these are available in Annex 2 of our statement on the transitional regulatory framework – <http://stakeholders.ofcom.org.uk/binaries/consultations/postal-regulation/statement/statement.pdf>

## Section 4

# The first Universal Postal Service Order

## The current universal service

4.1 The Act sets out in s.31 the minimum requirements of the universal postal service, which themselves implement the requirements of the EU Postal Services Directive<sup>20</sup> and Parliament's decision on what must be provided. The Act includes everything which was included in the definition of the universal service in the Postal Services Act 2000<sup>21</sup>.

4.2 The minimum requirements specified by the Act are:

### Requirement 1: delivery of letters or other postal packets

(1) At least one delivery of letters every Monday to Saturday—

(a) to the home or premises of every individual or other person in the United Kingdom, or (b) to such identifiable points for the delivery of postal packets as OFCOM may approve.

(2) At least one delivery of other postal packets every Monday to Friday to the places within paragraph (1)(a) or (b).

(3) The references in this requirement to the delivery of letters or other postal packets include the delivery of packets posted outside the United Kingdom.

### Requirement 2: collection of letters or other postal packets

(1) At least one collection of letters every Monday to Saturday from every access point in the United Kingdom used for the purpose of receiving postal packets, or any class of them, for onwards transmission in connection with the provision of a universal postal service.

(2) At least one collection of other postal packets every Monday to Friday from every access point in the United Kingdom used for that purpose.

(3) The references in this requirement to the onwards transmission of letters or other postal packets include their onwards transmission to places outside the United Kingdom.

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<sup>20</sup> Directive 97/67/EC as amended most recently by the Third Postal Directive 2008/6/EC, [http://ec.europa.eu/internal\\_market/post/legislation\\_en.htm#proposal](http://ec.europa.eu/internal_market/post/legislation_en.htm#proposal). The minimum requirements set out in the Act go beyond the requirements of the Directive by requiring a 6-day collection service rather than the 5-day requirement of the Directive and by requiring tariffs to be “uniform” in addition to affordable.

<sup>21</sup> Postal Services Act 2000, <http://www.legislation.gov.uk/ukpga/2000/26/contents>

Requirement 3: service at affordable prices in accordance with uniform public tariff

(1) A service of conveying postal packets from one place to another by post (including the incidental services of receiving, collecting, sorting and delivering them) at affordable prices determined in accordance with a public tariff which is uniform throughout the United Kingdom.

(2) The reference in this requirement to conveying postal packets from one place to another includes conveying them to places outside the United Kingdom.

Requirement 4: registered items service

A registered items service at affordable prices determined in accordance with a public tariff which is uniform throughout the United Kingdom.

Requirement 5: insured items service

An insured items service at affordable prices determined in accordance with a public tariff which is uniform throughout the United Kingdom.

Requirement 6: services to blind or partially sighted

The provision free of charge of such postal services as are specified in the universal postal service order to such descriptions of blind or partially sighted persons as are so specified.

Requirement 7: legislative petitions and addresses

A service of conveying free of charge qualifying legislative petitions and addresses.

4.3 Currently, DUSP 1 lists the products which Royal Mail must provide to discharge its universal service obligation. The current universal services are transposed from Royal Mail's former licence, and are, with the exclusion of those due to fall out of the service on 5 December 2011:

- First class stamped, single piece PPI and meter mail;
- Second Class stamped, single piece PPI and meter mail;
- Standard Parcels;
- Stamped, PPI and metered Airmail;
- Stamped, PPI and metered Surface Mail;
- Incoming services for letters posted outside the UK, together with a requirement to use reasonable endeavours to establish delivery arrangements with postal operators in countries outside the UK;

- Special Delivery Next Day (not on account);
  - International Signed For, when sold with single piece Airmail and Surface Mail services;
  - Redirections;
  - Keepsafe (from 6 December 2011);
  - Recorded Signed For;
  - Certificate of Posting;
  - Poste Restante;
  - Petitions and addresses.
- 4.4 In addition DUSP 1 requires one delivery of relevant postal packets to every home or premises and one collection of relevant postal packets from access points used in the provision of the universal service every working day. DUSP 2 covers the provision of free services for the blind and partially sighted.
- 4.5 The quality of service targets which are associated with these services are set out in DUSP 5, and are discussed in the next Section.
- 4.6 The Act also requires us in s.30 to “carry out an assessment of the extent to which the market for the provision of postal services in the United Kingdom is meeting the reasonable needs of the users of those services” before making or modifying a universal postal service order. This obligation does not apply for making the first order, but the Act requires us to conduct such a review within 18 months of vesting.

## **We propose to move to a description of universal services**

- 4.7 The Act establishes a regime in which Ofcom must, in effect, give more detail about what universal services should be provided, by requiring Ofcom under s.30 to make an order to set out:
- a description of the services that they consider should be provided in the UK as a universal postal service;
  - the standards with which those services are to comply.
- 4.8 An order under s.30 of the Act is a type of statutory instrument. Under s.63 of the Act and s.403 of the Communications Act, we must consult before making it but it is not laid before Parliament.

## **Regulatory Impact Assessment**

- 4.9 In the Regulatory Impact Assessment for the UPSO in Annex 7 we discuss the options to fulfil our duty. The first option is not to make an order, which would in practice mean that we would keep the current list of services in the conditions. We consider that this is not a feasible option, as we are under a clear legal obligation to make an order. The second option is to make an order describing the existing universal service. This is the proposal we make in this consultation document and we discuss it in more detail below. The third option is to make an order changing the

universal service, but we consider that we should carry out the review of user needs first, and in the meantime retain the essential features of the universal service.

- 4.10 Because the Act is clear that we need to move to a *description* of services, we therefore propose to set, out in the order, a description of the characteristics of the universal services, rather than a list of product names.
- 4.11 The current system has the advantage of certainty about which named services are part of the universal service – for instance, Special Delivery Next Day. However, there could arguably be some debate about the characteristics of the products and the terms and conditions which should be part of the product definition. The current list-based approach to providing more details about the composition of the universal service was sufficient to protect customers when Royal Mail needed approval to make non-beneficial changes to terms and conditions other than price.
- 4.12 However, we are also proposing to move away from the approval mechanism. In this context, it is important to have clarity about the features of the universal service to be protected, and our proposals are intended to ensure we can enforce the universal service obligation and protect the essential features of the universal service while making sure that Royal Mail can make appropriate changes if necessary.
- 4.13 The Act (section 33) sets out a series of exceptions to the minimum requirements of the universal service, including for geographical and other circumstances which Ofcom considers to be exceptional. Clearly, it is not possible for Ofcom to set out in the Order all the circumstances which Ofcom may consider to be exceptional. Due to a convention of the drafting of legislation, it is not possible to cross refer to a document which changes from time to time. Nor is it clear that section 30 authorises us to specify the exceptions in the order at all. We therefore propose that the UPSO will describe the universal service without any of the exceptions, which will remain as set out in section 33 of the Act and statements made by Ofcom identifying exceptional circumstances.
- 4.14 In proposing the change to a description of services we intend to retain all the essential features of the current universal service. As we stated in our proposals for the future framework for economic regulation “*the scope of the universal service will remain unchanged from the present scope*”, pending the review of user needs<sup>22</sup> and its implications, if any, for the universal service.
- 4.15 This is not to say that, from time to time, Royal Mail cannot make changes to some of the terms and conditions relating to universal service products. However, our focus is clearly on the importance of preserving the current universal service pending the review of user needs. The minimum requirements of the universal service cannot, in any event, be changed without approval from Parliament.
- 4.16 This consultation is an opportunity for us to test whether our proposals achieve our aim of maintaining the features of the current universal service. We particularly welcome feedback on both our general approach and the specific features of the universal service we propose to specify in regulation.
- 4.17 Moving to a description of the characteristics of the universal service will be better aligned with good regulatory practice because it will have the advantages of:

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<sup>22</sup> Our work on reviewing the needs of postal users must be completed by April 2013.

- **Clarity.** Currently, because the products within the universal service are defined by giving the name of the product, the definition of each product is not necessarily systematic or complete, and relies on the definition given by Royal Mail. This will clarify the characteristics necessary for Royal Mail to meet in order to fulfil its universal service obligation. Such clarity is beneficial to postal users, who will be able to refer to the characteristics to know what to expect of universal service products.
- **Focus.** This allows us and all interested parties the opportunity to consider the characteristics of the universal services and specify the ones which must be provided to meet the minimum requirements and which are necessary to reflect the current universal service products.
- **Flexibility.** In future, this move will allow us to move away from considering the universal service as a suite of products, towards identifying the characteristics which are important to customers. While retaining the current features of the universal service, this could give Royal Mail some limited flexibility to amend product terms and conditions where this is not essential to the current universal service. It paves the way for a more flexible approach to the composition of the universal service in future, should this become desirable.

4.18 As noted above we intend to ensure that the universal service remains essentially the same following the introduction of the first UPSO and new DUSP. In particular, we think this will be achieved by our approach of describing the essential characteristics of the services. If stakeholders consider that there are important characteristics of the universal service that we have not captured in our descriptions, this consultation is the opportunity to bring this to our attention.

4.19 Furthermore, in those areas where we are proposing Royal Mail should have greater commercial freedom regarding non-price terms and conditions for universal service products, we are proposing that all such terms are fair and reasonable. We are also proposing that Royal Mail must give one month's notice before changing prices or non-price terms and conditions for universal service products.

### Our proposals for characteristics of universal service

4.20 In summary we propose that the following characteristics should be specified:

- **Definition of the product.** This is to describe what a product mainly does, for instance, a postal service, or a service of redirecting mail.
- **Delivery and collections six days a week for letters, five for packets.** This is a minimum requirement of the Act.
- **Universal access.** This requires that any customer may post items from any access point, to every home and premises in the UK (or worldwide)<sup>23</sup>. This is a minimum requirement of the Act<sup>24</sup>.

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<sup>23</sup> Services for the blind would of course only be available to the blind.

<sup>24</sup> However, we note that there are sometimes operational restrictions, for instance the fact that the post must reach remote areas, which means that the product cannot be provided at the same specification for all UK addresses. For instance, Special Delivery Next Day is not available next day by 1pm in a small number of postcode areas. Another example is Redirections, which is not available

- **Uniform and affordable prices.** While we have proposed in the October consultation to give Royal Mail commercial freedom in setting prices for universal service products (with the exception of the price cap for Second Class stamps for standard letters), the prices for these products must be (a) the same regardless of destination within the UK (i.e. uniform) and (b) affordable. This is a minimum requirement of the Act.
  - **Single piece, where applicable** (in effect excluding products attracting presentation and volume discounts). For the purpose of the order, we consider that a single piece service means a postal service whose price (on average for each postal packet) is not subject to any discounts related to number of postal packets sent in connection with the person who paid for the service, the positioning of text on the postal packet, the use of markings which facilitate the use of machines to sort postal packets or the pre-sortation into geographical areas for delivery<sup>25</sup>.
  - **Speed and associated quality of service targets.** We consider that this is a key characteristic of the products. This would include, for instance, the guaranteed delivery by 1pm of Special Delivery Next Day<sup>24</sup>.
  - **Dimensions and weight.** These are specified by the UPU<sup>26</sup> and the Act<sup>27</sup>.
  - **Tracking.** Although it could be argued this is a commercial add-on to Special Delivery Next Day, it is currently an integral part of the service. We do not however propose to specify tracking for Recorded Signed For and International Signed For, which only have a partial tracking facility.
- 4.21 This covers the characteristics of postal services we identified as most important to the delivery of the universal service. Because we seek to preserve the essential characteristics of the universal service as it currently is, we identified these characteristics by including the requirements of the Directive and the Act and the current product description and terms and conditions. Annex 6 includes further details about the characteristics associated with the products currently provided as part of the universal service, Annex 9 includes a draft order and Annex 10 includes associated conditions.
- 4.22 We propose that Royal Mail's universal service products must match the characteristics we specify – but in order to provide commercial flexibility, their products need not be *limited* to these characteristics. In other words, it may be that their products (whilst meeting the essential features of universal services) also have additional features.

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in some situations, for instance for mail for people that were not occupying the old address, or mail addressed to boarding houses, hotels, colleges or other multi-occupied premises.

<sup>25</sup> This definition is based on the Postcomm definition of single piece expressed in its August decision on the universal service, with the following exceptions. The Postcomm definition excluded premium products (e.g. Recorded Signed For) from the definition, whereas we do not make this distinction. In addition, it excluded discounts related to payment channel whereas Ofcom's definition does not. Source: Postcomm, *Removing bulk products from the universal service and clarifying the status of other universal service products – a decision document*, August 2011, <http://stakeholders.ofcom.org.uk/binaries/post/2005.pdf>

<sup>26</sup> Section 33(1)(b) of the Act

<sup>27</sup> Section 33(1)(a) of the Act

- 4.23 In addition, it is difficult to anticipate all changes that Royal Mail may seek to make to the terms and conditions of the products provided as part of the universal service. As discussed in the next Section, we consider that the non-price terms of universal services should be fair and reasonable.
- 4.24 The recent applications from Royal Mail provide examples of the type of issues that could arise, such as a change to the retention period of undeliverable items, or Royal Mail's trial of the delivery of postal items to a neighbour where they cannot be delivered to an absent addressee because a signature is required or the item is too big to put through the letterbox<sup>28</sup>. In these instances, where we consider that there is a justifiable case for doing so, we can assess whether the proposed terms are fair and reasonable.
- 4.25 The characteristics which we propose not to specify are:
- **Price.** Specific prices are an issue discussed in our October consultation (focused on securing the provision of the universal service - it includes proposals to lift removes price controls but with a safeguard for vulnerable consumers via a price cap on Second Class stamped letters). An exception is where the Act requires certain services to be provided free (for example, services to the blind) or the same is true of the existing universal service as set out in condition DUSP 1 (for example, certificate of posting). We will specify that universal services must have a uniform and affordable price.
  - **Format of the items** i.e. letter, large letter and parcels, or *weight steps*. Royal Mail sets prices according to these formats. Therefore, to define format would be to intervene on pricing, whereas in the October consultation we are proposing Royal Mail should have commercial freedom to set prices (with the exception of the price for Second Class stamps for standard letters). Specifying format would be a form of intervention in pricing<sup>29</sup>. This does not relate to maximum weight or dimensions (e.g. length), which we will specify in line with the requirements of the Act and the UPU as described above.
  - **Requirements imposed on customers.** This is what Royal Mail asks of its customers when it performs the services, such as requiring a return address on Airmail envelopes, or specifying that the guarantee of Special Delivery Next Day does not apply if no-one is at the address. These seem to relate to operational and practical issues which do not appear to require regulation. There are some rare exceptions where we need to specify some of those requirements as part of the regulatory instruments, e.g. in relation to petitions, where unless we specify the presentation requirements the obligation may be drawn more widely than it is intended to.
- 4.26 In addition, we propose not to include the following features in the universal service products characteristics, because they can already be required in other regulatory conditions:
- **Compensation.** We believe the availability of compensation is important but we consider the issue of compensation separately, in Section 6 of the consultation document, as part of Consumer Protection conditions. We propose to require the

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<sup>28</sup> Postcomm, *Royal Mail Terms and Conditions Consultation Decision*, September 2011.

<sup>29</sup> We note again that specific prices are an issue discussed in our October consultation.



provision of reasonable compensation, where this is currently provided by Royal Mail for universal service products<sup>30</sup>.

- **Times of collection and delivery.** Times of collection and delivery have not previously been regulated directly as part of the universal service. DUSP (5.3) requires Royal Mail to notify us of the specified delivery and collection times from post boxes, any changes they intend to make to those times, and any reclassification which results in the collection time starting earlier. We propose to keep this notification requirement, as evidence suggests that times of delivery and collection, and in particular consistency of delivery times, are important to customers<sup>31</sup>.

*Q4.1 Do you agree that we have identified the correct characteristics of a universal service in order to ensure that the universal service remains essentially the same? If not please identify those characteristics that should or should not be specified in the order, and provide reasons.*

## Duration periods for Redirections, Keepsafe and Poste Restante

- 4.27 *Redirections*<sup>32</sup>, *Keepsafe*<sup>33</sup> and *Poste Restante*<sup>34</sup> are all services which can be requested from Royal Mail for a specific period of time, rather than being a “one-off” service. The current duration periods of these products are:
- a) *Redirections*: for periods of one month, three months, six months and 12 months, with the ability to renew redirection services for up to a maximum of two years from the commencement of the initial redirection service
  - b) *Keepsafe*: for any periods up to 66 days
  - c) *Poste Restante*: 14 days if the item was posted in the UK (including the Channel Islands and the Isle of Man), one month if it was posted overseas, two months if it is addressed to a post office branch at a sea port if the customer is arriving by ship.
- 4.28 We consider that the fact that these products are available for a period of time is an essential characteristic of the products: the value of the Redirection service relies on the fact that mail can be redirected over a certain period.
- 4.29 However, specifying the period for which these products must be offered by Royal Mail may be overly prescriptive, as Royal Mail would not be able to change the duration offered at all until and unless we made a change to the regulatory framework. This would set the current durations in stone for the near future and

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<sup>30</sup> By compensation here we mean “normal” compensation, other than the compensation required for insured and registered services. In respect of these services we propose to require a domestic and a cross-border insured and registered service(s) to be provided, in accordance with the Postal Services Directive and s.32 of the Act.

<sup>31</sup> See for instance Jigsaw Research, *Postcomm Customer Survey 2008*, February 2009, <http://stakeholders.ofcom.org.uk/binaries/post/93.pdf>. For instance, SMEs surveyed were resistant to later delivery times.

<sup>32</sup> Redirect mail from an old address to another address.

<sup>33</sup> A service which holds UK customers' mail at their local delivery office while they are away, and then delivers it on their return.

<sup>34</sup> Mail redirected to a chosen post office.

would remove Royal Mail's flexibility to make minor changes which could be beneficial to customers.

- 4.30 We therefore propose to specify that Redirections, Keepsafe and Poste Restante services should have a duration period. Specifying reasonable duration would ensure that customers continue to enjoy the service, as a reasonable period for the service must continue to be provided by Royal Mail, while allowing some changes to the period of time the service is currently offered, if necessary.

*Q4.2. Do you agree we should specify that the duration of redirections, Keepsafe and Poste Restante should be reasonable? If not, please provide your reasons.*

## Should redelivery, caller's service and return to sender be part of the Universal Postal Service?

### Redelivery and caller's service

- 4.31 Royal Mail's redelivery service for parcels, Special Delivery Next Day and Recorded Signed For means that a packet can be delivered to a local post office for collection by the customer, redelivered to another address within the same postcode, or redelivered another day to the original address.
- 4.32 Collection from the delivery office ("caller's service"<sup>35</sup>) is also available. Redelivery and collection from the delivery office are not currently mandatory for Royal Mail to provide.
- 4.33 While redelivery and caller's service are two distinct activities, for the purposes of this Section, we include caller's service in redelivery.

### Return to Sender

- 4.34 The return to sender service is the service whereby the customer receives a letter with the correct address but the wrong name, writes "return to sender" or "not known at this address" and puts it back in a pillar box or post office. Royal Mail then, where it is able to identify the sender, delivers it back to the sender<sup>36</sup>. Return to sender is currently required to be provided free of charge as part of a regulated product, in transitory condition, T 4.

### Should they be part of the universal service?

- 4.35 Neither redelivery nor return to sender will be required to be provided in the new regime if we do not actively decide that they are part of the terms of a universal service and therefore should be provided.

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<sup>35</sup> See Royal Mail's website for more information:

<http://www.royalmail.com/sites/default/files/docs/pdf/Callers%20Service%20Web%20December%2010.pdf>

<sup>36</sup> For more information on how Royal Mail deals with items which need to be returned see <http://www2.royalmail.com/customer-service/safe-and-sound>, <http://www2.royalmail.com/customer-service/getting-other-peoples-mail> and <http://www2.royalmail.com/customer-service/personal-customers/missed-deliveries/what-happens-dont-pick-item>.

- 4.36 It could be argued that the postal service is provided at the first attempt at delivery to the address, and everything else is additional – in which case redelivery or return to sender are not components of the current universal service products.
- 4.37 However, it could also be argued that delivery implies that the item has been transferred to the intended address, and that this is not achieved if there has not been some reasonable effort to ensure that the item reaches the addressee<sup>37</sup>. By reasonable effort, we mean one attempt at redelivery or collection by the customer. Royal Mail's current practice, and that of other parcel operators, seems to point in that direction.
- 4.38 In addition, we consider that:
- redelivery is an important aspect of the service for customers in that it enables those not available at the time of delivery to obtain their item; and
  - it is reasonable to expect Royal Mail to make provision to return the item to the original sender, who paid for the service, if the item is returned in the post. This does not impose an obligation on Royal Mail to return the item to the sender if Royal Mail introduces a choice for some products and the sender chooses not to have the item returned.
- 4.39 There is a risk that this constrains Royal Mail's commercial flexibility. However it does not impose additional regulatory requirements on Royal Mail, as Royal Mail currently needs prior approval of all non-price 'mandatory' changes to regulated services. In addition, Royal Mail will continue to be able to adapt to customer needs: the only thing required is one attempt at delivery and collection and one attempt at returning to sender, in the same way as Royal Mail currently provides it. Our proposal only applies to redelivery and return to sender of items sent using a universal service (such as, currently, First class).
- 4.40 In line with our proposals in October to provide Royal Mail with more flexibility<sup>38</sup>, we are not proposing to continue to require return to sender to be free of charge. This implies that Royal Mail could require payment by the sender even though they did not seek this service, although of course the terms and conditions should continue to be fair and reasonable, and we will continue to monitor the provision of the universal service products. Alternatively for items purchased at the post office, Royal Mail could introduce a specific, opt-in service<sup>39</sup>.
- 4.41 We would like to invite respondents' views as to whether redelivery and return to sender should be considered as part of the terms of the universal service products, or should not be specified.

*Q4.3 Do you agree redelivery and return to sender are part of the characteristics of universal services and should be specified in the order? Please also provide the reasons for your view.*

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<sup>37</sup>The Postal Services Directive replaced the term "delivery" by "distribution" in defining postal services. Distribution is defined as "the process from sorting at the distribution centre to the delivery of postal items to their addressees".

<sup>38</sup><http://stakeholders.ofcom.org.uk/binaries/consultations/securing-the-postal-service/summary/condoc.pdf>

<sup>39</sup> Royal Mail's current terms and conditions for undeliverable and re-posted letters can be found in the Inland Letter Post Scheme, <http://www.royalmail.com/sites/default/files/docs/pdf/ILPScheme.pdf>.

*Q4.4: Do you agree return to sender should not continue to be required to be provided free of charge? If not please provide your reasons.*

## **We propose that Royal Mail should publish and update a list setting out how it meets its universal service obligation**

4.42 We consider that it important for users and other operators to know which products are in the universal service, for which they can expect the safeguards associated with the universal service to apply (e.g. one price goes everywhere). This is also important for regulatory purposes (e.g. the future regulatory monitoring of Royal Mail) and VAT purposes, given that universal service products are VAT-exempt. We propose elsewhere in this document that Royal Mail should give one month's notification of changes to its universal service products.

### **Our proposals on notification**

4.43 To ensure certainty and transparency for postal users, we propose a notification regime for the products (that meet the characteristics) of the universal services which Royal Mail will be required to provide. We propose that:

- Royal Mail should publish a list of all the services which it provides as part of the universal service; and
- Royal Mail should update this list when there is a change. This includes taking out and replacing a product in the universal service (even if there is no change to product specification).

4.44 We do not expect that publishing a list of its universal service products (and updating that list when required) would be an onerous requirement on Royal Mail.

4.45 We invite views as to whether the notification period for changes to the list of universal service products should be:

- **One month.** This would be in line with our proposals for a minimum one month advance notification of non-price changes to the universal service (discussed in the next Section) and the same arguments apply - that it is likely that residential customers would not need more than one months' notice of price and the significant majority of non-price changes. And, as noted in the next Section, most businesses operate on a one month billing process and may therefore also require a minimum of one months' notice to pass any price increase on to their customers (see Section 5 for more details on arguments for one month's notice); or
- **Three months.** Given the importance of certainty to postal users of the composition of the universal service, for instance to know the VAT status of products, and given that Royal Mail will need reasonable time to implement the implication of changing the product composition of the universal service, a period of three months may be more appropriate.

*Q4.5 Do you think the notification period for changes to the list of services provided as part of the universal service should be one month, or three months?*

## Summary of our proposals

4.46 In summary we propose to:

- Focus on maintaining the features that customers currently expect from universal service products and ensuring that the universal service will remain essentially the same as now, pending the review of user needs;
- Move towards defining the universal service by describing its characteristics;
- Require Royal Mail to provide fair and reasonable (non-price) terms for universal service products, to capture those aspects of the universal service not proposed to be described (see also Section 5); and
- Require Royal Mail to publish a list of the universal services provided, and notify us and customers of any changes to that list (in Section 5, we also propose notification of non-price changes to universal services).

## Section 5

# Setting the conditions for the provision of the Universal Postal Service

- 5.1 This Section covers our approach to the DUSP conditions which apply to Royal Mail as the designated USP and relate to the provision of the universal postal service.
- 5.2 A DUSP condition may require the designated universal service provider to:
- Provide a universal service or part of a universal service, throughout the UK or in a specified area of the UK, in accordance with the standards set out in the Order;
  - Provide access points for the purposes of a universal postal service;
  - Provide specified information to postal operators and users about the universal services it is required to provide; and
  - Do anything else that Ofcom considers appropriate for the purposes of or in consequence of any of these obligations<sup>40</sup>.
- 5.3 In particular, a DUSP condition may make provision as to tariffs and may impose performance targets<sup>41</sup>.
- 5.4 Under s.37 of the Act, a DUSP condition must include provision requiring the designated universal service provider to publish information about the extent to which it is providing specified postal services in accordance with specified standards and to publish annually an independently audited performance report.
- 5.5 A DUSP condition may be imposed only if Ofcom considers it necessary to do so in order to secure the provision of a service of a description set out in the Order in accordance with the standards set out there<sup>42</sup>.
- 5.6 We discuss three proposed DUSP conditions in this Section:
- A broad condition to secure the provision of a universal service;
  - A condition that specifies the performance targets (quality of service requirements) for universal services; and
  - A condition to cover the provision of information to users of universal services. (including requirements for notification and publication of changes to the price and non-price terms of these services).
- 5.7 There are close linkages between our discussion of quality of service requirements for universal services and those that exist for non-universal services. Therefore although the latter requirements currently sit within a consumer protection condition

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<sup>40</sup> Section 36(2).

<sup>41</sup> Section 36(4) and (6).

<sup>42</sup> Section 36(3).

(CP 1), we believe it is relevant to also reflect on and set out our proposed approach to the quality of service requirements for non-universal services within this Section.

- 5.8 For similar reasons, we also discuss the publication and advance notification requirements for non-universal services within this Section.
- 5.9 We discuss our approach and proposals for each of these in turn – and then set out a summary of our proposals at the end of the Section.

## **Obligation to provide a universal postal service**

- 5.10 Under the previous regulatory regime the obligation on Royal Mail to provide the universal postal service was contained in licence condition 2. When we transposed Royal Mail's licence into the general authorisation regime, this obligation was transposed as initial condition DUSP1. As with licence condition 2 this initial condition sets out a list of the products that Royal Mail must provide as the USP.
- 5.11 As we have noted in the previous section, the Act requires us to describe the universal postal service in the UPSO. This order by itself does not impose a requirement on Royal Mail to provide the universal service. As set out above, under s.36 of the Act, Ofcom may impose a DUSP condition to impose this obligation on Royal Mail.

## **Our proposal**

- 5.12 We propose to require Royal Mail to provide the universal service, and to specify in more detail the characteristics of the universal service, by imposing a DUSP condition. In the order, and consequently DUSP 1, we propose to move away from a list of services to a description of the universal service based on the characteristics of the universal service and the products currently provided.
- 5.13 We are not proposing to change the current service, simply our approach to specifying it (see the previous Section for a discussion of the rationale behind this move, and the advantages and risks of our proposal).
- 5.14 As proposed in the previous Section, this condition will also require Royal Mail to publish a list of universal service products, and to notify us and customers of any changes.

## **Free services for the blind and partially sighted**

- 5.15 Under the previous regulatory regime, condition 6 of Royal Mail's licence referred to free services for the blind and partially sighted. We transposed this as initial condition DUSP2. This requires Royal Mail to provide to blind and partially sighted people the services specified by directions of the relevant Secretary of State<sup>43</sup> and to do so free of charge.
- 5.16 There is a different legal basis for this obligation in the Postal Services Act 2011 compared to the Postal Services Act 2000. In the 2000 Act Postcomm could only require Royal Mail to offer free services for the blind and partially sighted if so

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<sup>43</sup> Direction contained in Social and Environmental Guidance to the Postal Services Commission issued under section 43(2) of the Postal Services Act 2000 by the Secretary of State, March 2001, <http://stakeholders.ofcom.org.uk/binaries/post/356.pdf>

directed by the Secretary of State (s.41(2) of the 2000 Act). The 2011 Act made the provision free of charge of services for blind or partially sighted people one of the minimum requirements that must make up the universal postal service.

- 5.17 As noted in the previous Section the UPSO will require free services to blind and partially sighted people in accordance with the minimum requirements of the Act.

### Other free services

- 5.18 DUSP 1 currently requires *Certificate of Posting, Poste Restante* and *Petitions* to be provided free of charge.
- 5.19 We propose to retain the requirement for the USP to provide these services free of charge because they are currently part of the universal service, and we have committed to maintain the essential features of the universal service pending the review of user needs.
- 5.20 Return to Sender is currently required to be provided free of charge under T4, which is due to lapse at the end of March 2012. We discussed our approach to *Return to Sender* in the previous Section – asking whether it should remain part of the universal service. We also proposed that there should be no requirement to provide it free of charge going forward.

### Provision of access points

- 5.21 Under the previous regulatory regime, condition 3 of Royal Mail's licence imposed obligations upon Royal Mail to provide or procure the provision of access points for the universal service in a manner which meets the reasonable needs of users having regard to the costs of providing and servicing such access points.
- 5.22 We transposed this as initial condition DUSP3. This condition sets out the following:
- DUSP 3.1 sets out the general obligation that Royal Mail “shall provide, or procure the provision of, post office letter boxes and other access points for the purpose of providing the universal postal service ... which meets the reasonable needs of users having regard to the costs of providing and servicing such access points”;
  - DUSP 3.2 sets out a series of tests, which if it has met them, Royal Mail shall be regarded as having met its obligations under 3.1;
  - DUSP 3.3 sets out a requirement for Royal Mail to maintain a statement of the arrangements it has in place for users whose premises are more than 10km from an access point; and
  - DUSP 3.4 sets out a requirement for Royal Mail to maintain a statement of the arrangements it has in place for users who are blind or partially sighted, infirm through age, chronically sick, or disabled.



- 5.23 This initial condition meets our duty under s.29 of the Act<sup>44</sup> to require Royal Mail to ensure the provision of letter boxes and other access points for the purpose of providing universal services, e.g. Post Offices.

### **Density of postal office letter boxes in non-rural areas**

- 5.24 DUSP 3.2 sets out a test for the density of access points in non-rural areas. With regard to post office letter boxes it states:

“The Universal Service Provider shall be regarded as having met its obligations under DUSP 3.1 if – (a) in each postcode area where the delivery point density is not less than 200 delivery points per square kilometre not less than 99% of users of postal services are within 500 metres of a post office letter box”.

- 5.25 This obligation has been in place in the same form since 2001. However, in 2005, Royal Mail informed Postcomm that it was not meeting the density target in 29 of the 55 Postcode areas with more than 200 delivery points per square kilometre. At this time Postcomm considered:

“Royal Mail should focus upon the provision of access points so as to meet the reasonable needs of users rather than solely to hit the density target. The main purpose of the density requirement in Condition 3.2 in our view is to act as a methodology for assessing whether Royal Mail have complied with their obligation in Condition 3.1”.

- 5.26 According to the latest available data there are currently 121 Postcode Areas, of which 55 have more than 200 delivery points per square kilometres. Of these 30 meet the requirement set out in DUSP 3.2 that 99% of users of postal services are within 500 metres of a post office letter box. Of the 25 Postcode Areas that are not meeting the target:

- In 22 areas 97%-98% of users are within 500 metres; and
- In three areas 95%-96% of users are within 500 metres.

- 5.27 We understand that neither Postcomm, the National Consumer Council (Consumer Focus) nor Royal Mail have received any significant level of complaints about the density of post boxes in urban areas in the past. Furthermore a 2007 study commissioned by Postcomm suggests that post boxes are accessible: about two thirds of respondents perceived that they travelled for less than a quarter of a mile, and about 80% travelled to the post box they use most often by foot<sup>45</sup>.

- 5.28 Taking both the information set out above and Postcomm’s interpretation of the relationship between the obligations in DUSP 3.1 and DUSP 3.2 into account would suggest that Royal Mail is compliant with DUSP 3. However, we consider that it would be more transparent to review the density criteria imposed by DUSP 3.2.

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<sup>44</sup>OFCOM’s duty under s.29 of the Act includes a duty to “carry out their functions in relation to postal services in a way that they consider will secure the provision of sufficient access points to meet the reasonable needs of users of the universal postal service.”

<sup>45</sup> NERA, *Access to postal services – a final report for Postcomm*, August 2007, <http://stakeholders.ofcom.org.uk/binaries/post/1068.pdf>.

## Summary of proposal on DUSP3

- 5.29 We propose to retain DUSP 3 in its entirety as it fulfils an important role in meeting out duties under s.29 of the Act.
- 5.30 As we have yet to review the access criteria set out in DUSP 3.2, we propose to retain it in its current form to continue to meet our duty to secure the provision of sufficient access points to meet the reasonable needs of users, pending the review of user needs.
- 5.31 Therefore, we propose to consider the needs of postal users in accessing the universal service as part of the user needs review. We will assess whether the current density requirements are appropriate and, if not, what density requirements should replace them.

*Q5.1 Do you agree with a proposed condition to require Royal Mail to provide a universal postal service in line with specified characteristics, which requires them to meet specified standards; requires the provision of access points to particular criteria and which will now also require them to publish a list of universal service products, and to notify us and customers of any changes to that list? If not, please explain why.*

## Ensuring the quality of the universal postal service

- 5.32 In this subsection we discuss the conditions that are used to ensure the quality of the universal postal service.
- 5.33 We also discuss our approach to quality standards for non-universal services.
- 5.34 Initial condition DUSP5 (which transposed parts of licence condition 4 of the previous regulatory regime) requires Royal Mail to meet quality of service targets for its universal services.
- 5.35 There is also a consumer protection condition – ('CP 1') – which requires Royal Mail to meet quality of service targets for its universal and non-universal services.

## Effect of the quality of service conditions

- 5.36 Regulatory condition DUSP 5 sets out Royal Mail's quality of service (QoS) targets for universal services and its obligations regarding the measurement of performance against the targets. The condition also sets out the reporting and audit requirements for Royal Mail's QoS performance – for instance, there is a requirement for Royal Mail to provide quarterly and annual reports to Ofcom and Consumer Focus on whether it has achieved the targets.
- 5.37 In addition, part of CP 1 places similar obligations to DUSP5 on Royal Mail with regard to its quality standards for collection and delivery of universal and non-universal service postal packets and how it should report on the achievement of these standards. These services cover certain bulk mail products and the percentage of collection points (including business collections) service each day (CP 1.1).

## Quality of Service targets for universal services

### Current QoS targets and the incentive mechanisms

5.38 Royal Mail's current QoS targets for universal services are set out in a table to the Annex to Condition DUSP 5 and replicated below:

**Table 1- Current QoS targets for universal services<sup>46</sup>**

		Performance bands			
		I	II	III	IV
	DUSP scheduled services	Standard (%)	No automatic consequences (%)	Users receive price reductions (%)	Ofcom considers investigation (%)
1	<b>Grouping 1<sup>47</sup>:</b> Retail First Class	93.0	<93.0 but >92.0	92.0 to >88.0	88.0 or less
2	<b>Grouping 2<sup>48</sup>:</b> Retail Second Class	98.5	<98.5 but >97.5	97.5 to >93.5	93.5 or less
3	Standard Parcels	90.0	<90.0 but >89.0	89.0 to >85.0	85.0 or less
4	European International Delivery	85.0	<85.0 but >84.0	84.0 to >80.0	80.0 or less
5	Special Delivery (Next Day)	99.0	Compensation in accordance with contractual specification		94 or less
<b>DUSP standardised measures</b>					
6	<u>Postcode area target % (delivered)</u>	91.5	<91.5 but >90.5	90.5 to >86.5	86.5 or less
7	% of delivery routes completed each day	99.90	<99.90 but >99.80	99.80 to >99.40	99.40 or less
8	% of items <u>delivered correctly</u>	99.50	<99.50 but >99.40	99.40 to >99.00	99.00 or less

5.39 There are currently two mechanisms in the regulatory conditions to incentivise the achievement of QoS targets. First, Royal Mail must use all reasonable endeavours to meet such targets, failing which it can be subject to investigation and sanction if performance falls below certain levels (DUSP 5.4) - (band IV in Table 1 above).

5.40 Secondly, the transitory condition which sets the current price control features a QoS incentive mechanism ('C-factor') whereby, if Royal Mail fails its QoS targets for some

<sup>46</sup> Standard parcels is a Second Class service, European International Delivery refers to Airmail Europe, the postcode area target is for 91.5% of First Class stamped and metered mail to be delivered by the next working day in 118 out of 121 postcode areas – HS (Hebrides), KW (Kirkwall) and ZE (Lerwick) are exempt due to their remoteness.

<sup>47</sup> Grouping 1 relates to retail stamped and metered First Class.

<sup>48</sup> Grouping 2 relates to retail stamped and metered Second Class.

of its retail products and standardised measures<sup>49</sup> (outside a certain deadband), permissible price rises in subsequent years are lower than would otherwise be the case (T4.13)<sup>50</sup>. The “price reductions” in performance band III in Table 1 refer to this QoS incentive mechanism in the price control.

- 5.41 In addition, there are QoS targets in initial condition CP 1 for some of Royal Mail’s non-universal services. For example, CP 1 includes targets for bulk mail services that are currently price controlled. CP 1 also includes a target for 99.9% of collection points to be served each day. Although daily collections from post offices and post boxes are in the universal service, the measurement of performance against this target currently includes business collections which are not in the universal service. Therefore, this target is currently in initial condition CP 1 rather than DUSP 5. However, please see pages 35-36 for our discussion and proposals on moving *collections* QoS from CP 1 to DUSP 5.

## **The reliability and quality of the universal postal service are fundamental**

### **We propose to maintain the quality of service targets for universal services**

- 5.42 In this subsection we now discuss our proposed approach to ensuring the reliability and quality of the universal postal service going forward. We noted in the previous Section on the UPSO that we propose to require Royal Mail to provide universal services to specified standards.
- 5.43 We consider that it is important for Royal Mail to achieve its QoS targets. Many of the current targets were developed from Royal Mail’s own internal targets and have been in place since 2001. Historical performance suggests that all of the targets are achievable.
- 5.44 We consider it would be most appropriate to consider the specific level of these targets as part of the comprehensive review of user needs which will be completed by April 2013. In the meantime, we believe the current targets should remain in place and Royal Mail should be obliged to continue to meet them through a DUSP condition on performance targets for universal services.
- 5.45 Instead, this subsection discusses what we may do if the targets are not achieved which is an effect – and subject to the outcome – of our October consultation<sup>51</sup>.

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<sup>49</sup> % of collection points served each day, % of delivery routes completed each day, % of items delivered correctly and a postcode area target which requires Royal Mail to deliver 91.5% of first class retail items by the next working day in 118 postcode areas.

<sup>50</sup> The C factor mechanism came into effect in 2006 and historically, adjustments were made due to quality of service failures subject to Postcomm’s consideration of Royal Mail’s applications for exemptions due to force majeure and/or transformation-related industrial action.

<sup>51</sup> This subsection also does not consider the compensation customers can get for specific failures. Section 6 covers compensation arrangements. Following negotiations with Postcomm, Royal Mail put in place voluntary compensation arrangements for individual items of mail that are lost or damaged and Royal Mail also provides compensation for delay. The arrangements are not automatic and payment is not linked to overall performance against the quality of service targets. Customers must apply for compensation for each item that is lost, damaged or delayed and will only be successful if their application meets the specific criteria set by Royal Mail (for example, the claimant must provide proof of posting and proof of value for items with intrinsic value).

- 5.46 In that earlier consultation, we proposed to grant Royal Mail commercial freedom for a period of seven years by not imposing a traditional price control but subject to a number of safeguards. One of the safeguards is monitoring and the potential for re-regulation. Under this safeguard, we will focus in particular on monitoring performance against QoS targets to ensure that the universal service continues to be provided at the level required and that the service that users receive is maintained to the required standard. Another safeguard is to ensure that a basic universal service product is available to all and affordable to all, via a safeguard cap for Second Class stamps discussed in Section 8.

### **The effect of our proposals in the October consultation**

- 5.47 Our proposals in the October consultation, if implemented, would mean that the C-factor mechanism in the price control, which is currently in transitory condition T4.13, will cease to apply from 1 April 2012 (alongside the price control mechanism itself). [As the C-factor makes adjustments to prices in the year following the QoS failures, the removal of the current price control from 1 April 2012 actually means that C-factor adjustments will not be applied to any failures in the current QoS reporting year of April 2011- March 2012].
- 5.48 For clarity, this means that the last three performance bands on page 32 – performance bands II, III, IV – will fall away. In turn, this means that if Royal Mail were, in future, to miss their QoS targets, then we would be able to consider what action to take.
- 5.49 The QoS table targets we propose to include in a regulatory condition are therefore those set out in the table within Annex 10.

### **We consider that the risk of investigation and enforcement action will incentivise Royal Mail to meet its quality of service targets for universal services**

- 5.50 For Royal Mail's QoS performance in 2011-12 and subsequent years, the proposed cessation of the price control and associated C-factor mechanism means that if Ofcom considers that any corrective action is required due to Royal Mail failing its QoS targets, then it would be undertaken through enforcement of the relevant regulatory condition and would follow the general procedures in Schedule 7 of the Act.
- 5.51 We believe that this regime should provide sufficient incentive for Royal Mail to perform but also allow Ofcom to take appropriate action where targets are not achieved.
- 5.52 Before deciding whether to start an investigation for QoS failures, Ofcom may take into consideration any exceptional circumstances e.g. *force majeure* events, such as the recent volcanic ash incidents, which may have had an impact on Royal Mail's performance.

### **Implications for quality of service requirements now bulk mail and business collections are confirmed as non-universal services**

- 5.53 As noted above, we discuss within this Section our approach to the QoS requirements for non-universal services. This is due to a recent decision by

Postcomm about what is – and what is not – within the scope of the universal postal service.

- 5.54 In August 2011, Postcomm issued a decision document<sup>52</sup> which removed bulk mail (Mailsort 1400 and Cleanmail) products from the universal service. The main reasons given for removal were as follows:
- An important element of the original rationale to include these products in the universal service was their high usage and the fact that Cleanmail was considered an entry level bulk product for small businesses. Postcomm found that these factors appeared less relevant today. In particular, Cleanmail and Mailsort 1400 are less used now than they were in 2003-04. Also these products were not necessarily used by small businesses and the D+2 and later markets are increasingly competitive, with the result that alternative bulk mail products are now available to an increasing range of business customers.
  - Bulk mailers appear more attached to low prices than the distinctive features of the universal service.
  - Royal Mail would be unlikely to stop providing these services as long as it retains its universal service obligation in relation to single piece items, as the additional revenue from bulk products far outweighs the incremental costs of providing them.
- 5.55 In the same decision document, Postcomm also confirmed that business collections are not in the universal service.
- 5.56 Postcomm's decision document did not explain what would happen to the associated QoS targets for bulk mail and daily collections (which currently includes business collections) and the requirement on Royal Mail to include business collections in its measurement of the percentage of collections made at or after the final time of collection advertised on the access point.

**We propose to remove quality of service targets and reporting obligations for Royal Mail's retail bulk mail services and business collections as they are no longer universal services**

- 5.57 We are required by the Directive and Act to specify quality standards, and the publication of these, with respect to universal services. We are not required to do so for services falling outside the universal service.
- 5.58 Accordingly, and in keeping with our presumption against intervention, we propose that quality standards and reporting should be limited to universal services and the obligation to meet and report against targets for bulk mail services and business collections should be lifted.
- 5.59 In CP 1 there is currently a singular "collection points served each day" target of 99.9%, plus a requirement for Royal Mail to report on the percentage of collection points made after the final time advertised on the access point. The measurement of

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<sup>52</sup> Postcomm *The building blocks for a sustainable postal service - Removing bulk products from the universal service and clarifying the status of other universal service products – a decision document* August 2011 <http://stakeholders.ofcom.org.uk/binaries/post/2005.pdf>

performance against these includes both business collections and collections from universal service access points (i.e. post offices and post boxes).

- 5.60 We propose to remove business collections from the “collection points served each day” target and the collections times reporting requirement so they only relate to collections from universal service access points and place these requirements (more appropriately) into the DUSP on performance standards to sit alongside the QoS requirements on universal services. We understand it would be possible for Royal Mail to measure and report on QoS for collections from post offices and post boxes only without undue cost, as they did so pre-2007.
- 5.61 For bulk mail, we propose the removal of the bulk QoS targets which means those that exist for bulk First Class, bulk Second Class and bulk Third Class. This would mean the measurement, auditing and reporting mechanisms associated with these targets would not be required for regulatory purposes.
- 5.62 It should be noted that Royal Mail’s bulk compensation scheme for delay is currently aligned with performance against the regulated QoS targets for bulk mail. If the regulated targets are removed as a result of this consultation, Royal Mail will have to consider how its bulk mail compensation scheme for delay will operate in the absence of regulated targets. As the bulk mail compensation scheme for delay is not regulated, Ofcom will have no oversight of any changes that Royal Mail may wish to make.
- 5.63 In relation to the impact of removing quality standards and reporting for non universal services:
- for bulk mail, Royal Mail will be free to set its own service quality levels; and
  - for paid for business collections, Royal Mail will be free to set its own service quality levels. Royal Mail can remove business collections from its measurement of the percentage of collection points served each day and collections times performance.
- 5.64 We consider that Royal Mail will still have incentives to offer and maintain appropriate service levels for these services as required by its customers even if we do not set regulated QoS targets. We believe the incentive is provided by Royal Mail’s need to offer or maintain services at levels that satisfy customers who might otherwise consider switching to alternatives, e.g. access-based competitors or non-postal forms of communication.
- 5.65 We consider our proposal to remove QoS regulation from non-universal services is aligned with our proposals in the October consultation to give Royal Mail more commercial freedom. It is also aligned with Postcomm’s conclusion<sup>52</sup>, which we agree with - that increasing competition (plus the fact that revenues from bulk mail are fundamental to the sustainability of Royal Mail’s business) - means that users’ needs in relation to bulk mail should be met by the market itself and therefore bulk mail customers do not require the safeguards provided by its inclusion in the universal service. The removal of QoS regulation would also promote a more level playing field across operators providing similar services.
- 5.66 In light of the above, we propose to remove all reference to QoS targets and reporting of QoS performance for bulk mail services by:
- deleting CP 1.1, CP 1.3, CP 1.5 to CP 1.8, CP 1.10 and the Annex to CP 1;

- deleting the reference to CP 1.1 and CP 1.10 in CP 1.18;
- deleting the reference to CP 1.1 in CP 1.21;
- deleting the wording “the standards in the schedule and” in CP 1.22;
- deleting the references to “the standards in the schedule or” which appear three times in CP 1.23;
- deleting the wording “the schedule or” in CP 1.24; and
- deleting the wording “schedule and” in CP 1.25.

5.67 We would also include the monitoring requirement currently at CP 1.4 and 1.7 and the reporting and publication requirement currently at CP 1.10(a) within the DUSP condition on service standards.

### Monitoring of access services

5.68 We should also note that CP 1 requires Royal Mail to:

- Monitor its performance in the provision of access services; and
- Report on its performance for access services in terms of the percentage of letters delivered by the end of the first working day after the day of collection or receipt.

5.69 We believe these requirements – in CP 1.9 and CP 1.11 – should (like our approach to bulk mail and business collections) be removed on the same basis that these are not universal services.

5.70 However, we would note that in Section 9 we discuss our proposals for the access condition and, as part of these proposals we do propose that the USP access condition includes a requirement for Royal Mail to provide its customers with QoS information based on a fair and reasonable system of monitoring QoS.

*Q5.2 Do you agree with our proposed condition which specifies universal postal service performance standards? If not, please explain why.*

### Contingency planning

5.71 Initial condition DUSP 4 (which transposed licence condition 3 part II of the previous regulatory regime) requires Royal Mail to maintain appropriate contingency plans which ensure as far as practical the provision of the universal service without interruption, suspension or restriction of any service in the event of local, regional or national industrial action, emergencies or natural disasters.

5.72 Royal Mail must also conduct a review of its contingency plans at least every two years and provide Ofcom with a report on this<sup>53</sup>. Should Ofcom be of the view that

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<sup>53</sup>In practice, this biennial review has taken the form of a meeting between Royal Mail and the regulator to discuss any developments in respect of Royal Mail’s contingency plan policy making that Royal Mail considers should be highlighted to the regulator.



the contingency plans should be modified in any way, Royal Mail is under a “comply or explain” obligation.

- 5.73 DUSP 4.2 also requires that Royal Mail must maintain a list showing how it will prioritise its provision of its services in the event of the type of events noted above<sup>54</sup>. This essentially specifies how Royal Mail should go about ensuring that it meets its overall obligation to provide universal services (save in cases of emergency or in the case of exceptional circumstances specified by Ofcom). If the priority list is amended, Royal Mail is required to notify Ofcom within one month of the change.
- 5.74 As outlined in earlier in this Section, we propose to continue to require Royal Mail to provide universal services to certain standards, and in the event of failure, we will be able to investigate such failures, and, if appropriate, take enforcement action. We have considered what this means for the requirements in DUSP4.
- 5.75 Firstly, we provisionally believe it is still appropriate to continue to retain a regulatory obligation requiring Royal Mail to maintain contingency plans in order to ensure the provision of the universal service. This high level requirement can help to provide an assurance that appropriate planning will be undertaken by Royal Mail in order to meet its obligations, including daily collections and deliveries across the UK to the required standards, and help ensure there is *continuity* in the provision of universal services.
- 5.76 We propose to reframe the requirement slightly so that Royal Mail is required to maintain ‘*appropriate*’ contingency plans. We would retain the obligation for Royal Mail to review its contingency plans at least every two years (under DUSP4.4) and we could therefore, in future, use our information gathering powers to establish the outcomes of its reviews and, in addition, require Royal Mail to potentially amend its contingency plans (if ever necessary) to make them more appropriate. As a result, we propose to delete DUSP 4.5 and 4.6 which currently obliges Royal Mail to send us a report following their biennial review of contingency plans (and to consider altering their plans following an Ofcom request).
- 5.77 In line with the current clause at DUSP4.3, we would require Royal Mail to implement its contingency plans in the event of emergencies - and in the event this did not happen, we would expect them to be able to explain why this was the case, taking into account the exact nature of the circumstances.

### **We propose to remove the requirement to maintain a priority list**

- 5.78 However, we also believe that Royal Mail should be provided with some flexibility for dealing with different challenges on service continuity. As a result, we consider that Royal Mail should no longer be required to maintain a list showing how it prioritises its provision of services and the criteria it applies to determine how the provision of services is to be prioritised. We believe it is an operational matter for Royal Mail to decide how to prioritise its resources and services, in order to meet its contractual obligations and requirements on the provision of the universal service. We recognise too that its prioritisation process may also need to vary depending on the particular nature of the issue causing the contingency plans to be deployed.

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<sup>54</sup>In practice, this has consisted of Royal Mail maintaining a list and notifying the regulator within one month of any change to the list.

- 5.79 As a result, we propose to delete DUSP4.2 (on the requirement to maintain a priority list) and also the references in other DUSP4 clauses to the *priority list*.

#### Impacts of removing requirement on the priority list

- 5.80 We do not anticipate our proposed change – to remove requirements on the priority list - would have any material impact on Royal Mail’s ability to ensure continuity of services although there may be a small reduction in the regulatory burden on Royal Mail.
- 5.81 Furthermore, if Ofcom decides to investigate any universal service failure it will be able to require Royal Mail, under its information gathering powers, to provide relevant details of how the company dealt with emergencies, industrial action etc and how and in doing so, why Royal Mail chose to prioritise services, on a case by case basis.
- 5.82 We note that under Ofcom’s penalty guidelines, in the calculation of any penalty for breach of a regulatory condition, we would take into account factors including:
- Whether in all the circumstances appropriate steps had been taken by the regulated body to prevent the contravention;
  - The extent to which the contravention occurred intentionally or recklessly, including the extent to which senior management knew, or ought to have known, that a contravention was occurring or would occur; and
  - Whether the contravention in question continued, or timely and effective steps were taken to end it, once the regulated body became aware of it.

*Q5.3 Do you agree with our approach to DUSP4 – which means Royal Mail would have to maintain appropriate contingency plans but will have no regulatory requirements in relation to a priority list? If not, please explain why.*

## **Provision of information to users of universal services**

- 5.83 The following subsection sets out Ofcom’s proposed approach to the notification and publication requirements for price and non-price terms and conditions for Royal Mail’s retail universal services. It also presents our proposed approach to any changes to the terms and conditions of universal services that Royal Mail seeks to make.

### **EU Directive and Postal Services Act 2011**

- 5.84 The Directive requires the UK to ensure that users and postal service providers are “regularly given sufficiently detailed and up to date information by the universal service provider regarding the particular features of the universal service offered, with special reference to the general conditions of access to those services as well as to prices and quality standard levels”.
- 5.85 The Act allows Ofcom to impose a designated USP condition “to provide specified information” to “other postal operators and users of postal services” about the universal services it is required to provide. In addition, it allows Ofcom to impose a consumer protection condition requiring a postal operator to “establish and maintain procedures, standards and policies with respect to consumer protection matters”.

## The current condition

- 5.86 The consumer protection condition 4 (previously licence condition 7) applies to Royal Mail only and covers both universal and non-universal services. We discuss our proposed approach to the requirements for retail non-universal services later in this Section.
- 5.87 Royal Mail as the USP has to provide Ofcom and Consumer Focus a statement on:
- Details of tariffs, standards of service and compensation arrangements under which Royal Mail provides specified postal services<sup>55</sup>;
  - Details of the physical provisions and conditions for access to such specified services;
  - Details of any services offered by the USP specifically for customers who are blind, partially sighted, disabled or chronically sick, of pensionable age, with lower incomes or residing in rural areas; and
  - A summary of the operation of Royal Mail's standards of service compensation scheme and its compensation scheme for loss and damage (under CP 1.16).
- 5.88 Under CP 4, Royal Mail is required to notify and publish changes to this information three months in advance (with the exception of some limited services exempted by direction). This includes any new specified postal services and/or bespoke or individually negotiated services. There is an exemption in place for contracts won through competitive tenders, although Royal Mail is required to publish summary details of such contracts.
- 5.89 In addition, under transitory condition 4.3, Royal Mail must apply to Ofcom if it wishes to make non-beneficial non-price changes to regulated services. This includes all price controlled services, miscellaneous services (such as redirections) and non-priced services (such as services for the blind). Ofcom can then, after consultation, direct Royal Mail not to make its proposed changes.

## Links to our October consultation

- 5.90 We note that this document should be read in conjunction with our October consultation. In that earlier document we set out our view of the need for Royal Mail to have more flexibility<sup>2</sup>. To this end we proposed removing the significant majority of price controls for Royal Mail's universal service and access products.
- 5.91 It can be argued that the notification and publication requirements that Royal Mail is currently subject to also reduce its flexibility to respond to its customers' needs in a timely manner. We have therefore considered what the appropriate balance should be between protecting customers and giving additional commercial flexibility to Royal Mail.

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<sup>55</sup> Specified postal services in the current regulatory condition means the conveyance from one place to another (including the incidental services of receipt, collection and delivery) of postal packets.

## Advance notification and publication requirements for changes to the price and non-price terms of Royal Mail's universal services

### Publication of prices and terms and conditions

5.92 There is currently very little (if any) competition for customers of universal service retail products and this is unlikely to change in the medium term. It is therefore essential that standard terms and conditions and prices are published to ensure all customers can access these products. This is also a requirement of the Directive. We are therefore proposing to require Royal Mail to continue to publish up-to-date price and non-price terms and conditions for universal services and ensure these are accessible for all customers. We consider that universal services by their definition need to be available to all customers and as such any bespoke arrangements which Royal Mail agrees with its customers cannot be defined as universal services.

### Advance notification requirements

5.93 The Directive does not expressly require advance notice of any changes to terms and conditions. It is however clear that notice on the day of a change may in practice not provide sufficient notice for many customers<sup>56</sup>. We have therefore considered the advance notice that universal service customers need, particularly given the majority of customers are captive, and assessed this against the benefits of giving additional commercial flexibility to Royal Mail.

### Residential users

5.94 Given the low average weekly household expenditure on postal services<sup>57</sup>, we consider that it is unlikely that residential customers will need to change their spending or budgeting habits to accommodate postal price increases. However, Royal Mail does not currently put the cost of postage on the First and Second Class standard letter stamps. If this continues, it is likely that some customers will want to insure themselves against the price increase through the purchase of stamps in advance of the price change coming into effect.

5.95 In the past, the vast majority of non-price changes notified by Royal Mail have been for non-universal services. In addition, the most commonly used universal services do not place significant presentation requirements on customers, such as specifying the font used for the receiving address or sorting the mail in a specified order. Therefore, many non-price changes will not require residential customers to change the way they purchase postal products.

5.96 However, it is likely that some non-price changes could require residential customers to be given notice to change their behaviour<sup>58</sup>, and in some cases the notice period may need to be significant and accompanied by an effective communication campaign as it is difficult for Royal Mail to communicate to these customers given their diversity and geographic spread.

5.97 We therefore consider it is reasonable that Royal Mail provides at least some advance notice of price and non-price changes to residential customers. The length

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<sup>56</sup>See also Recital 14.

<sup>57</sup>On average, UK households only spend 40p on post each week, which equates to around 0.1 % of total income.

<sup>58</sup>Such as pricing based on the format of letters/packets (i.e. not just weight).

of the notice period required by residential customers is likely to depend on the nature of the price or non-price change being implemented. Any notice period that Royal Mail is required to give universal service customers should be considered a minimum and we would expect Royal Mail to give more notice to its customers where this is required to meet the reasonable needs of those customers.

### Business users

- 5.98 Universal service products are also used by the majority of business customers. Larger businesses use universal services for small and ad hoc mailings, with the majority of their mail sent using bulk mail products. Many small and some medium sized businesses have no choice but to use universal services as they do not meet the minimum volume criteria for either Royal Mail or other operators' bulk mail products. We have therefore also considered the length of the notice period required by business customers and small to medium businesses in particular.
- 5.99 In their responses to Postcomm's previous consultations on notification and publication requirements, business customers have expressed their concerns about the potential impact that reduced notification periods would have on their ability to plan and budget effectively and potentially to pass on any Royal Mail price increases to their customers. While this requirement may be less important for universal services, given the lower volumes sent, we consider it is likely business customers will still need some notice to plan and budget for price changes (and where necessary and possible pass on this price increase to their customers).
- 5.100 In addition, as noted above non-price changes to universal services are likely to require less operational changes than non-universal services (due to the lower presentation requirements). However, it is likely that businesses will require some advance notification to enable them to implement any modifications required from Royal Mail's non-price changes.

### **We propose that the appropriate minimum notice for any future changes to the price and terms of Royal Mail universal services is one month**

- 5.101 We have considered a range of options for the minimum advance notification requirement for retail universal services from the current three month period to 24 hours (as was used in the telecoms market until recently)<sup>59</sup>.
- 5.102 One month is often used in other industries as the minimum period to protect consumers and is the notice that telecommunications providers are required to give for materially adverse changes<sup>60</sup>.
- 5.103 We consider that residential customers would not need more than one month's notice of price and the significant majority of non-price changes.
- 5.104 Businesses are likely to require notice to communicate and implement price changes to their customers (for example for postage and packaging). Most businesses operate on a one month billing process and may therefore also require a minimum of one month's notice to pass any price increase on to their customers. We recognise

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<sup>59</sup> Telecoms operators are now only required to notify their customers of a price change once it has come into effect.

<sup>60</sup> General Condition 9: Requirement to offer contracts with minimum terms. See <http://stakeholders.ofcom.org.uk/binaries/telecoms/ga/general-conditions.pdf>.

that some businesses cannot pass increased postal costs on to their customers in the short to medium term. However, this is likely to remain the case for some businesses even if the current three month notice period applied and it is important to consider the impact of this against the benefits of giving Royal Mail additional commercial flexibility.

- 5.105 We are therefore proposing that the appropriate notice period for price and non-price changes should be one month. This should give customers sufficient time to make any operational adjustments required by non-price changes. This would be a minimum requirement and we would expect Royal Mail to give more notice to customers if a change was likely to have a significant impact.

### Impact of this proposal

- 5.106 This proposal would give Royal Mail more commercial flexibility to make changes to its price and non-price terms for universal services in a timely manner. It should therefore be able to better meet the needs of its customers for non-price changes. Royal Mail has informed us that it requires three months to implement price changes to its internal systems for universal services. Therefore, we do not expect that it would have a significant impact on its ability to change universal service prices to react to market changes in the short to medium term.
- 5.107 In practice we do not expect our proposal to reduce the notification and publication period for universal service price and non-price changes to have a significant impact on residential customers. As noted above, residential customers on average have a very low spend on postal services and as such less notice of price changes is not likely to have a significant impact (and in any event Royal Mail is likely to give three months' notice of price changes for the foreseeable future).
- 5.108 This proposal would give business customers using universal services less time to react to price and/or non-price changes than the current three month period. However, as noted above it is likely that Royal Mail would give more notice of changes that would have a significant impact on its customers. In addition, if Royal Mail uses this additional flexibility to better meet the needs of its customers in a timely manner then it may have a positive impact for all universal service customers.

*Q5.4 Do you agree with our proposal to reduce the notice period for price and non-price changes to universal services to one month? If not, please provide evidence to support your view.*

## **The prior approval process for changes to the non-price terms for universal services**

- 5.109 As set out above, Royal Mail is currently required to apply to Ofcom if it wishes to make changes that are considered non-beneficial to the terms and conditions for its regulated services<sup>8</sup>. The current process requires consultation with Consumer Focus and sometimes more widely. It can take several months, even if the changes are accepted, and could be considered a barrier to Royal Mail making changes to its product mix and innovating. However, it is also important that customers are protected from degradation of the universal service.
- 5.110 As discussed in Section 4, we are proposing to describe the universal service rather than list the individual Royal Mail services that make up the universal service. This means that the core characteristics of the universal service will be set out in the

universal postal service order and these will be protected. Royal Mail would also be required to notify the products it has chosen to provide as universal service products and any changes to the list of universal service products in advance. In addition, it would only be able to make changes to the terms and conditions that were not considered essential to the universal service and as such were not specified in the UPSO.

### **We propose to remove the prior approval process for such changes to the non-price terms of universal services**

- 5.111 We do not consider it is appropriate to place any additional requirements on Royal Mail to seek approval for any changes to its universal services that are not specified in the UPSO.
- 5.112 However, we do consider that the non-price terms of universal services should be fair and reasonable. Hence, we propose to include a requirement on Royal Mail to ensure that the terms and conditions for its universal service are fair and reasonable once the current approval obligation falls away. Customers would be able to complain to Ofcom if they considered any changes were not fair and reasonable.

#### Impact of this proposal

- 5.113 This proposal should give Royal Mail additional flexibility to make changes to its universal services in a timely manner. This will allow it to make changes to its portfolio of products in response to market changes and customer needs within the specifications set out in the UPSO.
- 5.114 As noted above we intend to ensure that the universal service remains essentially the same following the introduction of the first UPSO and new DUSP. Therefore we do not anticipate that the additional flexibility we propose for Royal Mail will have a significant impact on customers. However, the proposed change would mean that any changes to the UPSO and DUSP condition flow through directly to increased flexibility for Royal Mail.
- 5.115 As noted above we are proposing that Royal Mail will only need to give one month's notice of non-price changes for universal services. We would also expect that Royal Mail would be working closely with its customers to ensure that the terms and conditions for any changes to its universal services are fair and reasonable and we can investigate, in the event that this does not happen.

*Q5.5 Do you agree that, given we will now be defining the characteristics of universal services, we should not impose prior approval requirements on Royal Mail for non-price changes to the universal services? If not, please provide evidence to support your view.*

### **Summary of our proposals on requirements for changes to the price and non-price terms of Royal Mail's universal services**

- 5.116 Given the analysis and evidence above we are proposing the following approach<sup>61</sup>:

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<sup>61</sup> We note that if implemented, the changes proposed in this section will not come into effect until 1 April 2012. Royal Mail will continue to be subject to the three month advance notification requirement for changes to both universal (and non-universal services discussed in Section 6) until this date. If

- a) That Royal Mail publish (and make accessible) the prices and terms and conditions for all universal services;
- b) That Royal Mail give one month's advance notice of changes to price and non-price terms for universal services; and
- c) Not to impose any requirements on Royal Mail to get approval from Ofcom for any changes to universal services (which are not specified in the UPSO); and
- d) That Royal Mail ensures the non-price terms and conditions for universal services are fair and reasonable.

### **Publication and advance notification requirements for Royal Mail's retail non-universal services**

5.117 CP 4 also includes a requirement for Royal Mail to publish both price and non-price terms for the significant majority of retail non-universal services and any changes to these terms three months in advance of implementation. We now discuss our proposal for this requirement given that we have just discussed our approach to notification and publication requirements for universal services above.

5.118 The requirement under CP 4 for the notification and publication of current and proposed price and non-price terms for non-universal services includes any bespoke services, although there is an exemption from the advance notification for contracts won through competitive tenders<sup>62</sup>.

5.119 Royal Mail has consistently stated that these requirements prevent it from being responsive to its customers' needs and are not necessary<sup>63</sup>. Whereas, customers and customer interest groups have in the past strongly objected to proposals by Postcomm to reduce publication notice periods.

### **We propose to no longer require Royal Mail to publish prices and terms and conditions or give advance notice of changes to the price or non-price terms of its retail non-universal services**

5.120 Our primary duty under the Act is to carry out our functions to secure provision of the universal service. The focus of many of our proposals is to relax the current regulatory controls on products and services which do not form part of the universal service, in order to allow Royal Mail greater flexibility in the market.

5.121 As noted earlier in this Section none of these retail products are within the scope of the universal service. It is therefore our view, consistent with our overall proposed approach, that it would be appropriate not to impose onerous obligations for such

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Royal Mail wishes to introduce price changes in the beginning of April 2012, as it has done in the past, these prices will need to be notified and published three months in advance. This will be before the close of the consultation period of the proposals for the future economic framework and this consultation. However, this will not prohibit Royal Mail from issuing its prices in the meantime on the proviso that these may be subject to change due to Ofcom's decisions on these proposed changes.

<sup>62</sup> In practice Royal Mail has won very few competitive tenders over the current price control period.

<sup>63</sup> See

<http://webarchive.nationalarchives.gov.uk/20111027102050/http://www.psc.gov.uk/documents/1990.pdf>.



non-universal products. To retain these obligations would significantly reduce Royal Mail's commercial freedom on non-universal service products.

- 5.122 There is no regulatory requirement on Royal Mail to continue to provide any non-universal services and under the Act Ofcom is not able to implement a price cap on these services. It would therefore seem inconsistent to place notification and publication requirements on Royal Mail in respect of these services. In addition, Royal Mail has noted that it needs additional commercial flexibility to meet the needs of its customers and for example implement changes or bespoke contracts requested by customers once they have been agreed.
- 5.123 Furthermore, the majority of customers for most retail non-universal services have greater choice of operator at least for the provision of upstream activities (e.g. collection and trunking)<sup>64</sup> than universal service customers, i.e. from access operators.
- 5.124 However, we recognise that the length of notice for price and some non-price changes that some non-universal service customers receive can have a significant impact on their businesses. In the past customers and customer interest groups have strongly objected to proposals on this issue. In particular they have stated the impact that this could have on their ability to budget and plan effectively, including the ability to pass on the additional cost to customers and implement any operational changes that are necessary<sup>65</sup>.
- 5.125 Additionally, some retail non-universal service customers do not currently have any choice of operator and this is unlikely to change, at least in the medium term<sup>66</sup>. This includes First Class bulk mail customers as well as rural, smaller and more ad hoc bulk mail customers, although some of these customers may switch some of their mail to non-postal alternatives.
- 5.126 Retaining the current consumer protection condition would address these customer concerns, i.e. continuing to require Royal Mail to publish standard price and non-price terms. Some of Royal Mail's concerns could be addressed by requiring fair and reasonable notice rather than a set period; and by excluding individually negotiated contracts from the scope of the condition.
- 5.127 Having considered the issues above, we propose to lift the publication and advance notification requirements for Royal Mail's retail non-universal services and to monitor Royal Mail's performance in this area as part of our monitoring regime (including any complaints from customers). However, we recognise that this proposal represents a substantial potential change for the industry. Therefore, we are interested in

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<sup>64</sup> Postcomm estimated in that operators competing upstream with Royal Mail in the D+2 and later markets have a 63% share pre-sorted letters by volume, a 52% share in high volume unsorted letters by volume and a 37% share of high volume unsorted large letters by volume. There are currently 19 operators that hold access agreements with Royal Mail Wholesale.

<sup>65</sup> For example, the DMA has previously noted that direct mail campaigns can often take 10-12 weeks to complete and publishers have noted the difficulties in passing on increased postage costs to their customers.

<sup>66</sup> For example, Postcomm found limited actual or potential for competition in the next day delivery market (see <http://webarchive.nationalarchives.gov.uk/20111027102050/http://www.psc.gov.uk/documents/1158.pdf>) and customers in rural areas (see <http://webarchive.nationalarchives.gov.uk/20111027102050/http://www.psc.gov.uk/documents/1016.pdf>).

stakeholder views of retaining a requirement to publish price and non-price terms and to give fair and reasonable notice of any changes to these and substantive evidence of any potential detriment that our proposals would impose on individual customers and the market as a whole.

### Impact of this proposal

- 5.128 We consider that this proposal would give Royal Mail a significant amount of commercial freedom to better meet the needs of its customers and respond to changes in the market. The majority of changes that Royal Mail has made to non-universal services in the past few years have been beneficial or non-mandatory changes that could have been implemented immediately with no impact on any other customers. The removal of these requirements should have a positive benefit for customers wanting to negotiate different or better terms with Royal Mail.
- 5.129 While this proposal represents a significant reduction in the information that Royal Mail is required to give to its non-universal service customers, in practice we would expect it not to have a significant impact on customers. We would expect that Royal Mail will continue to publish its price and non-price terms for retail non-universal services as this is the most effective way for it to communicate with these customers.
- 5.130 As set out in Section 9, we are proposing that Royal Mail is required to give 10 weeks' notice of access price changes and is also required to give an appropriate notice period for non-price changes for access services<sup>67</sup> to allow access operators and Royal Mail retail to give sufficient notice to their customers. Therefore, if retail customers place significant value on a notice period for price and non-price changes to non-universal products, Royal Mail would have a commercial incentive to continue to provide sufficient notice in order to meet its customers' needs in order to compete with access operators. There is more of a risk that Royal Mail will not give sufficient notice of price and non-price changes to its smaller rural and/or ad-hoc customers as these customers are less likely to have a choice of operator.
- 5.131 In summary, we think that the need to communicate effectively with its customers and to compete with access operators will give Royal Mail sufficient incentives to provide its customers with sufficient information on its prices and terms and conditions and any changes to these within a reasonable time frame. We believe that Royal Mail is aware of the needs of its customers and as a commercial business it will continue to publish its standard price and non-price terms for non-universal services and that absent a regulatory requirement the market will determine the level of notice that should be given to customers.
- 5.132 While the retention of a consumer protection condition on Royal Mail to publish prices and terms and conditions and give fair and reasonable notice of any changes would provide an additional apparent safeguard for non-universal service customers, we consider it would add little as we believe Royal Mail is likely to have sufficient incentives to do this anyway. However, it would likely involve additional costs for Ofcom, and potentially Royal Mail, regarding ongoing compliance.
- 5.133 Therefore, we consider that on balance the risks of Royal Mail providing no (or detrimentally little) notice are low and outweighed by the benefits for Royal Mail and its customers of greater commercial flexibility.

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<sup>67</sup> Unless otherwise agreed between the parties.

- 5.134 Other operators may be concerned about the removal of the advance notification and publication requirements for bespoke retail contracts. This may reduce the opportunity for other operators to identify and complain to Ofcom about any anti-competitive behaviour by Royal Mail. However, as part of our proposals on regulatory financial reporting, Royal Mail would be required to publish some information on its separated accounts and provide further information to Ofcom. In addition, the details that Royal Mail currently publishes of any bespoke or individually negotiated contracts won are limited.
- 5.135 As set out in our October consultation and as discussed in Section 9 in this document, we are proposing to impose a requirement on Royal Mail to meet a margin squeeze test. This test would also apply to bespoke contracts and if implemented should ensure that Royal Mail does not engage in any anti-competitive behaviour in respect of the affected services.
- 5.136 We therefore consider that this proposal would not have a significant impact on other operators' ability to identify any anti-competitive behaviour.

*Q5.6 Do you agree with our proposal not to impose any notification and publication requirements on Royal Mail in respect of retail non-universal services? If not, please provide evidence to support your view.*

## Summary of our proposed changes to the DUSP conditions

- 5.137 We propose the following changes to create a DUSP condition which:
- requires the USP to provide the universal service essentially as it is now, in line with specified characteristics of the universal service and in accordance with specified standards;
  - includes an obligation on Royal Mail to provide free services for the blind and partially sighted;
  - require the USP to publish a list of universal service products, and to notify us and customers of any changes to the list; and
  - requires provision of access points to particular criteria.
- 5.138 We propose to create a DUSP condition covering universal service performance standards, which will maintain current universal service QoS targets. [We would be able to investigate at any point if these annual QoS targets were not achieved]<sup>68</sup>;
- 5.139 We propose to create a DUSP condition which covers the provision of information to users of universal services. This new condition would require Royal Mail:
- To publish the prices and terms and conditions for all universal services - and to give one month's advance notice of changes to price and non-price terms for these services; and

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<sup>68</sup> And as noted on page 36 the "collection points served each day" performance target would now also relate purely to collections from universal service access points (not business collections) - as would the requirement to measure and publish on a quarterly basis the percentage of collections from access points *made at or after the final time of collection advertised on the access point*.

- To ensure that non-price terms and conditions for its universal services are fair and reasonable.

5.140 We also propose to remove requirements for publication and advance notification for Royal Mail's retail non-universal services.

5.141 Finally, we propose to delete the current requirement for Royal Mail to maintain a priority list (in the condition on contingency planning).

## Tests for imposing a DUSP condition

5.142 The Directive requires the UK to ensure that the universal service it prescribes is "guaranteed" and requires steps to be taken to "ensure" the provision to users of sufficiently detailed and up to date information. Under s.29 of the Act Ofcom is under a duty to secure the provision of the universal postal service.

5.143 The universal service currently comprises services which the market does not independently provide, particularly not throughout the UK at a uniform affordable tariff. We do not consider that absent regulatory intervention the universal service would be provided to the required standards and we therefore consider it necessary to impose a DUSP condition in order to secure the provision of the services set out in the UPSO in accordance with the standards set out there.

5.144 We believe imposing a condition requiring provision of the universal postal service would be:

- **Objectively justifiable** because we must move to a description-based set of universal services and as we propose that the condition should maintain the features that customers *currently* expect from universal service products and ensure that the universal service will remain essentially the same as now. In terms of the new notification process for a list of universal service products, we believe this is required to provide transparency for users and allow us to ascertain if changes to that list comply with the characteristics we propose for universal services;
- **Not unduly discriminatory** because the change necessarily affects the USP – and there is only one such USP (Royal Mail) in the UK;
- **Proportionate** because we are not prescribing additional or reduced requirements for the universal services at this stage - only a simple notification process for the list of products which should not be an onerous requirement on Royal Mail; the imposition of a DUSP condition is the least onerous means of securing the provision of these services; and
- **Transparent** because it is clear that the change is intended to define the characteristics of universal services while safeguarding universal service provision in essentially its current form pending a full review.

5.145 We believe imposing performance targets in a DUSP condition would be:

- **Objectively justifiable** because we must specify quality standards for universal services. We are also proposing to retain existing performance targets for universal services and ensure the quality and reliability of these services. The removal of targets for bulk mail and business collections from CP 1 is justified on the basis that these are not universal services – and similarly, moving the QoS

target for 99.9% of collection points to be served each into this DUSP and only including collections from universal service access within this measurement is justified since business collections are no longer part of the universal service; and

- **Not unduly discriminatory** because the condition affects the USP – and there is only one such USP (Royal Mail) in the UK;
- **Proportionate** because we are not proposing to change the targets for the universal services specified in the condition so the proposal should not be an additional burden on Royal Mail. Similarly, universal service consumers should continue to be protected essentially as they are today. In addition, we believe Royal Mail will have incentives to maintain standards for non-universal services absent a regulatory requirement so it is not proportionate to extend this regulatory requirement to those services; and
- **Transparent** because it is clear that we impose performance targets for universal services in order to secure that they are provided to a sufficiently high standard.

5.146 We believe removing the priority list requirement in the contingency planning condition is:

- **Objectively justifiable** because it is important to provide some flexibility given the relative prioritisation of services may partly depend on the particular nature of the issue causing the contingency plans to be deployed;
- **Not unduly discriminatory** because Royal Mail is the only USP and operator who currently faces this requirement;
- **Proportionate** because Royal Mail should have an incentive to prioritise universal services anyway in order to meet its regulatory requirements as the USP (including related QoS standards) or risk enforcement action - and so it would not be proportionate to retain this regulation; and
- **Transparent** because it is clear that we are removing an unduly interventionist requirement.

5.147 We believe the proposed condition setting out the requirements on Royal Mail for the provision of information on universal postal services is:

- **Objectively justifiable** because the vast majority of universal service customers have no choice of operator apart from Royal Mail and therefore need to be given up to date information on universal services in order to access the services. Both residential and small business users are likely to require some notice to respond to both price and non-price changes;
- **Proportionate** because it balances the need for residential and small business customers to have notice of price and non-price changes to universal services against Royal Mail's requirement for additional commercial flexibility to respond to market changes and the needs of its customers. The changes to the specification of the universal service and requirement for terms and conditions to be fair and reasonable should provide sufficient protection for customers from unreasonable changes without an additional and potentially time consuming approval process;

- **Not unduly discriminatory** because Royal Mail is the designated universal service provider and is the only operator servicing the vast majority of universal service customers; and
- **Transparent** because the requirements are clearly linked to the goal of ensuring customers have sufficiently up-to-date information about universal services.

5.148 We believe the proposed removal of requirements covering publication and also advance notification of changes to the terms of **non**-universal postal services is:

- **Objectively justifiable** given the level of competition for the majority of non-universal services Royal Mail should be incentivised to publish and give sufficient advance notice of any changes if this is important to its customers;
- **Proportionate** because the market can reasonably be expected to meet customers' needs - and so it would not be proportionate to impose additional regulation;
- **Not unduly discriminatory** as Royal Mail is the only operator who currently has requirements to publish prices and terms and conditions; and
- **Transparent** as we have clearly set out our proposal to remove this requirement.

## Section 6

# Conditions required to protect consumers

- 6.1 This Section covers our approach to the one essential condition which applies to RPOs and the nine consumer protection (CP 1-9) conditions whose requirements vary in terms of their coverage, applying either to all postal operators, or all RPOs or just to Royal Mail.
- 6.2 We discuss our approach to the following requirements in this Section:
- The obligation for RPOs to use reasonable endeavours to collect postal packets as agreed with customers and deliver them appropriately within a reasonable time;
  - Compensation arrangements for Royal Mail's universal services;
  - The obligation on other RPOs (i.e. not Royal Mail) relating to them measuring and reporting on their contract targets;
  - The condition which covers Postal Common Operational Procedures (for handling misdirected or mis-collected mail or misdirected enquiries) and which applies to all RPOs;
  - The consumer complaints handling, reporting and redress requirements which apply to Royal Mail and to other postal operators; and
  - The essential condition on mail integrity, which applies to all RPOs.
- 6.3 We set out whether (and how) we propose changes to each of these in turn – and summarise our proposals at the end of the Section.

## Consumer protection and essential conditions

- 6.4 Both a consumer protection condition under s.51 of the Act and an essential condition under s.49 of the Act may be imposed on every postal operator or on every postal operator of a specified description.
- 6.5 A consumer protection condition is one requiring the operator to:
- Assume specified liability in respect of specified loss of or damage to specified postal packets;
  - Establish and maintain procedures, standards and policies with respect to consumer protection matters; and
  - Make payments towards the costs of Consumer Focus and Consumer Direct<sup>69</sup>.
- 6.6 An essential condition is one containing obligations for or in connection with the following purposes:

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<sup>69</sup> The Office of Fair Trading ('OFT') currently funds and manages Consumer Direct.

- safeguarding confidentiality in connection with the sending, conveyance and delivery of letters;
- safeguarding security where dangerous goods are transported;
- safeguarding the confidentiality of information conveyed;
- guarding against the theft or loss of or damage to postal packets; and
- securing the delivery of postal packets to the intended addressees.

### **Requirements for collecting postal packets ‘as agreed with customers’ and delivering postal packets within a reasonable time**

- 6.7 In this subsection, we propose further changes to consumer protection condition 1 (in addition to those which we set out in relation to quality standards within the previous Section).
- 6.8 CP 1.2 (previously in condition 4 of Royal Mail’s licence and condition 2 of the standard licence) places an obligation on all RPOs in relation to regulated postal services to use reasonable endeavours to:
- a) collect postal packets from their customers as agreed with them; and
  - b) deliver appropriately, or procure the delivery of, any postal packets they receive in the course of their business as a postal operator, within a reasonable time.
- 6.9 The MCF in its response to the August consultation on the transition to new regulatory framework<sup>70</sup> argued that it was unnecessary to include this requirement in any form in the initial conditions as market forces drive the required service levels.

### **Contractual and competitive drivers can help sustain service levels for collections and deliveries**

- 6.10 The wording “as agreed with them” in the broad requirement at CP 1.2(a) implies that this only applies to customers who have a contract with an RPO. Our provisional view is that contractual remedies should be sufficient to ensure that RPOs provide the required services for collection.
- 6.11 Similarly CP 1.2(b) requires all RPOs to “deliver appropriately”, or procure the delivery of, any postal packets they receive in relation to regulated postal services within a reasonable time. Our provisional view is that universal service customers will be protected by the universal service requirements in relation to delivery and for non-universal services, contractual remedies and competition should help drive RPOs to provide an adequate delivery service in order to retain customers.
- 6.12 We note that Postcomm did not have to enforce these obligations – on receipt of any evidence suggesting they were being breached.

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<sup>70</sup> The MCF response can be found here:

[http://stakeholders.ofcom.org.uk/binaries/consultations/postal-regulation/responses/Mail\\_Competition\\_Forum.pdf](http://stakeholders.ofcom.org.uk/binaries/consultations/postal-regulation/responses/Mail_Competition_Forum.pdf)



- 6.13 Postcomm also carried out annual business customer surveys. One aspect of the surveys was to monitor awareness, use and satisfaction with RPOs and Royal Mail. In 2009, the survey noted that those business customers using RPOs, other than Royal Mail, gave a satisfaction score of 7.9 out of 10<sup>71</sup>. Royal Mail scored an average of 7.8 out of 10.
- 6.14 The Mail Integrity code of practice (required by E 1) is intended to reduce the exposure to the risk of loss, theft, damage and/or interference in relation to regulated postal packets in the course of collection, conveyance and delivery. Additionally, the Common Operational Procedures Code of Practice (required by CP 5) and Common Operational Procedures Agreement are intended to minimise the risk of mis-posted, mis-collected or mis-directed code letters not being repatriated to the correct RPO, customer or addressee.
- 6.15 In relation to deliveries, we also note that the Act also amended the PSA 2000 to clarify when a postal operator can detain a packet – in respect of unpaid or underpaid postage or where a customs handling charge is applied.

#### Link to CP 5 – Postal Common Operational Procedures Code

- 6.16 If CP 1.2 were to be removed, a change may be required to CP 5 - the condition which requires RPOs to comply with the Postal Common Operational Procedures **Code** and be a party to the Postal Common Operational Procedures **Agreement**)<sup>72</sup>. Sections 4 and 5 of the Code require operators to route mis-posted, mis-directed and mis-collected letters variously to the relevant operator, the customer or the addressee, as appropriate.
- 6.17 However, currently, the Code only applies to packets weighing no more than 2kg for RPOs who are party to a USP Access Agreement, or else to letters weighing less than 350g where an item is being sent by a RPO not acting in the capacity of an Access Party<sup>73</sup>. This means the Code does not apply to (some) postal packets other than letters.
- 6.18 We can see no logical reason to limit the Code to parcels weighing no more than 2kg under the new regulatory framework. Nor do we see a reason for the Code to be restricted to only RPOs handling access mail rather than any access operator<sup>74</sup>. The purpose of the Code is to protect customers and ensure there are arrangements in place to route mis-posted, mis-collected or mis-directed items to the relevant operator, customer or addressee.
- 6.19 We believe that the Code should offer the above protection where there is most likely to be the opportunity for mail to be mis-collected, mis-directed or mis-posted. We believe the most likely places for mis-collection, mis-direction or mis-posting to occur are in a multi-operator environment, in particular where customers use more than one party to send mail. A customer may use an RPO, Royal Mail and an access

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<sup>71</sup>Postcomm, 2009 Business Customer Survey Summary.

<sup>72</sup>We note Royal Mail's assertion in response to our consultation on the conditions to apply from vesting that not all those who ought to be a party to this agreement in fact are – see <http://stakeholders.ofcom.org.uk/consultations/postal-regulation/?showResponses=true> . However, if a person who ought to be a party to the agreement is not, that is in itself a regulatory breach against which Ofcom could take enforcement action.

<sup>73</sup>An access party is defined as a postal operator (other than a universal service provider) which is party to an access agreement.

<sup>74</sup>An access operator is referred to in the Code as an access party.

operator for different types of its mail. Access operators now carry approximately 40% of mail but not all are currently covered by the Code. It therefore seems appropriate to require all such operators to also be party to the processes in place for mis-posted, mis-collected or mis-directed code letters to be repatriated to the correct operator, customer or addressee. We believe that the Code should continue to apply to RPOs providing regulated postal services. We do not consider that the Code should be extended to cover other end to end providers at this stage as their items are less likely to be mis-posted (as they are above 350g and therefore unlikely to be mis-posted in a Royal Mail letterbox), more likely to be tracked and such operators will be directly accountable to their customers.

- 6.20 Therefore, we propose to amend the Postal Common Operational Procedures Code of Practice (which is an Annex to CP 5) to ensure any postal packet<sup>75</sup> sent via Royal Mail or an access party, plus any letter<sup>76</sup> sent by an RPO that costs no more than £1 to send or weighs less than 350g, are covered by the mis-directed, mis-posted or mis-collected provisions. To effect this change, we have also proposed a change to the definition of access agreement<sup>77</sup>.
- 6.21 We note that consequential amendments will be required to the Postal Common Operational Procedures Agreement in light of the proposed changes to the Code. We will work with the signatories to the Agreement to secure the appropriate amendments to the current Agreement, using the existing change control procedures. Should this not be possible, it may be necessary for us to require postal operators to sign a new agreement to ensure the Agreement and Code are aligned.

#### Link to E 1 – the Mail Integrity Code

- 6.22 If CP 1.2 were to be removed, a change may also be required to essential condition 1 ('E 1') - the condition which requires RPOs to comply with the Mail Integrity Code. The Mail Integrity Code, which is annexed to E 1, is intended to reduce the exposure to the risk of loss, theft, damage and/or interference in relation to regulated postal packets in the course of collection, conveyance and delivery.
- 6.23 However, currently, the Code only applies to RPOs offering an end-to-end postal service. This means the Code does not apply to any access operators acting as such, including those access operators which are RPOs.

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<sup>75</sup> Postal packets and letters are defined for these purposes in accordance with their definitions in the Act (sections 27(2) and 65(1) respectively), subject to the proviso that they exclude postal packets which are excepted under section 33(1) of the Act and postal packets that contain items which it is reasonable to exclude from carriage by post and which do not comply with conditions reasonably imposed on their carriage by post by reason of their potential harm to health, public security or compliance with law.

<sup>76</sup> Ibid.

<sup>77</sup> In order to reflect the arrangements currently in place and to simplify the definition of who is covered (for example, by removing the defined terms "Intermediary" and "USP Access Agreement"), we are proposing to define an access agreement as (i) an agreement between postal operators under which one postal operator provides access to its postal facilities to the other for the partial provision of a postal service; and (ii) an agreement between a postal operator and a user of postal services where the user has entered into an agreement with Royal Mail for access to its postal facilities. The definition in (ii) is intended to ensure that the Code applies to access operators when providing postal services to customers who have entered into Customer Direct Access Agreement or Agency Operator Agreement with Royal Mail.

- 6.24 We can see no reason for the Code to be restricted to only RPOs rather than any access operator. The purpose of the Code is to protect customers and ensure there are arrangements in place to minimise the risk of loss, theft, damage and/or interference with code postal packets. As we have discussed above, in a multi-operator environment where customers use more than one operator there is scope for mistakes to arise. As set out above, access operators carry approximately 40% of mail, and as they are handling mail it seems appropriate to require such operators to also be party to the processes in place for mail integrity.
- 6.25 We believe that the Code should continue to apply to RPOs providing regulated postal services and to be extended to apply to access operators. We do not consider that the Code should be extended to cover other end to end providers, such as parcel couriers, at this stage as their items are more likely to be tracked and such operators will be directly accountable to their customers. Without such a common requirement across postal operators, there may be a risk that consumers lose confidence in the postal system as there could be less consistency in the levels of security afforded to their mail when conveyed across the postal delivery chain.
- 6.26 Therefore, we propose to amend the Mail Integrity Code to ensure any postal packet sent via Royal Mail, an RPO or an Access Operator is covered by the mail integrity provisions.

**We propose that the regulatory requirement CP 1.2 be removed (and propose amendments to the Postal Common Operational Procedures Code and Mail Integrity Code)**

- 6.27 In light of the above, we propose to remove CP 1.2 as we believe contractual remedies and market forces should provide the collections and delivery services demanded by customers- in conjunction with the proposed change to the Postal Common Operational Procedures Code of Practice (to secure appropriate re-routing of misdirected and mis-collected postal packets) and the Mail Integrity Code.

Impact of our proposals

- 6.28 We believe *the impact on* consumers of removing the requirement at CP1.2 is likely to be minimal as contractual obligations and market forces should continue to drive RPOs to meet the agreed collection and delivery requirements.
- 6.29 We believe the impact of extending the Postal Common Operational Procedures Code of Practice and Mail Integrity Code will be positive for consumers and the industry as it will ensure that suitable arrangements are in place for the security of mail and its correct repatriation of mis-posted, mis-collected or mis-directed packets. The evidence from Postcomm's work overseeing the Postal Common Operational Procedures Code of Practice, Postal Common Operational Procedures Agreement or the Mail Integrity Code does not indicate that these obligations place onerous requirements on relevant parties. The Codes currently apply to all regulated postal operators, many of whom are sole traders with significantly smaller businesses than access operators and the requirement to comply with these Codes has not prevented the development of smaller regulated postal operators. Our expectation is that the requirements will be consistent with good business practice.
- 6.30 We acknowledge that the impact of extending the Postal Common Operational Procedures Code of Practice and Mail Integrity Code may impose some additional costs for operators – however we expect that these would be outweighed by the important consumer benefits (as it will ensure that suitable arrangements are in place

for the security of mail and the correct repatriation of mis-posted, mis-collected or mis-directed packets).

6.31 We believe we can also mitigate any impacts from removing CP 1.2 as we:

- intend to carry out regular market research in relation to business mailers which will help us to monitor awareness, use and satisfaction with RPOs and Royal Mail;
- both Ofcom and Consumer Focus have information gathering powers should information be needed on RPO performance; and
- the Postal Common Operational Procedures Code of Practice requires each RPO to provide Ofcom with annual details of the number of misdirected code letters for which it was the receiving operator.

## Summary of proposed changes to CP 1.2

6.32 In light of the above, we propose to:

- Remove CP 1.2 – both clauses (a) and (b); and
- Make related amendments to the Postal Common Operational Procedures Code annexed to CP 5 and also to the Mail Integrity Code in E 1.

*Q6.1 Do you agree with our proposal to delete the requirement in CP 1.2 and the related changes to the PCOPC and Mail Integrity Code? If not, please explain why.*

## Royal Mail's compensation arrangements

6.33 Under the previous licence regime, requirements in relation to compensation arrangements were placed on Royal Mail, which were transposed into initial condition requirements as follows:

- CP 1.12-1.15 requires Royal Mail to maintain a standards of service compensation scheme for compensating users of postal services affected by a delay to an individual postal packet as specified in a "Standards of Service Compensation Scheme of Royal Mail Group Ltd";
- CP 1.16-17 requires Royal Mail to
  - publish a report on its operation of the standards of service compensation scheme and its compensation scheme for loss and damage; and
  - to review the standards or the compensation scheme and consider modifications made by Consumer Focus which are in the interest of users.

- 6.34 The “standards of service compensation scheme” in CP 1.12 refers to the retail compensation scheme for delay. The current arrangements are detailed on Royal Mail’s website<sup>78</sup>.
- 6.35 Royal Mail also has compensation arrangements for loss and damage which are included in its schemes made under section 89 of the Postal Services Act 2000 and compensation arrangements for specific (contractual) products in the terms and conditions of that product, for example for Redirections<sup>79</sup> and Keepsafe<sup>80</sup>.
- 6.36 CP 2 requires any postal operator to meet their obligations under any schemes made under section 89 of the Postal Services Act 2000. Schemes made under section 89 of the Act may relate to any terms and conditions of the postal service but, in particular, may set out the liability the operator assumes for loss and damage to postal packets. Currently Royal Mail is the only postal operator to make schemes under section 89<sup>81</sup>. Its inland and overseas letters and parcels schemes include, amongst other things, the current compensation arrangements for loss and damage for most of its universal services. The compensation arrangements for universal services that are not in the section 89 schemes are set out in Royal Mail’s specific terms and conditions for those products.

### The legal framework

- 6.37 Absent regulatory intervention, s.90 of the Postal Services Act 2000 provides that in relation to a universal service and in relation to any service for which the postal operator has made a s.89 scheme, a postal operator is not liable in “tort”<sup>82</sup> for any loss or damage a person suffers due to failure to collect a postal packet or due to anything done or omitted to be done to a postal packet in the course of transmission by post. This makes it difficult for a sender to claim compensation for loss or damage to their mail.
- 6.38 Under Article 19 of the Directive, the UK is required to ensure that postal service providers have appropriate procedures for dealing with postal users’ complaints, including provision, where warranted, for a system of reimbursement and/or compensation.
- 6.39 This has been implemented in the UK via section 51 of the Act, which allows Ofcom to impose consumer protection conditions. Amongst other things, a consumer protection condition may require an operator to assume specified liability in respect of specified loss of or damage to specified postal packets, and to establish and maintain procedures, standards and policies with respect to consumer protection matters which include the provision of remedies and redress for matters the subject of complaints. Section 52 of the Act allows Ofcom to require operators to be members of an approved redress scheme, while Schedule 5 of the Act prohibits Ofcom from approving a redress scheme unless it can require its members to provide minimum types of redress including paying compensation.

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<sup>78</sup> <http://www.royalmail.com/customer-service/personal-customers/refunds-and-compensation/claims-process/compensation-tables/compensation-delayed>

<sup>79</sup> [http://www.royalmail.com/sites/default/files/docs/pdf/Redirections%20Social%20December%2010.p](http://www.royalmail.com/sites/default/files/docs/pdf/Redirections%20Social%20December%2010.pdf)

<sup>80</sup> [http://www.royalmail.com/sites/default/files/keepsafe\\_agreement.pdf](http://www.royalmail.com/sites/default/files/keepsafe_agreement.pdf)

<sup>81</sup> <http://www.royalmail.com/customer-service/terms-and-conditions/non-contract-terms-and-conditions>

<sup>82</sup> Tort is a legal term which encompasses negligence, for example.

## The services for which compensation is warranted

- 6.40 Currently, Royal Mail's retail compensation arrangements for loss, damage and delay cover some but not all universal services. The following universal services are covered:
- First class stamped and metered mail;
  - Second class stamped and metered mail;
  - Standard parcels;
  - Recorded Signed For when using the above services;
  - Articles for the Blind; and
  - Special Delivery Next Day (not purchased on account)
- 6.41 In addition, the retail compensation for delay also covers items sent using any of the above services that have been redirected using Royal Mail's Redirections service.
- 6.42 Royal Mail's overseas letters and parcels schemes sets out, amongst other things, the compensation arrangements for loss and damage to international outbound services that are in the universal service. Namely:
- Airmail;
  - Surface mail; and
  - International Signed For.
- 6.43 Royal Mail's Redirections<sup>83</sup> and Keepsafe<sup>84</sup> services are in the universal service but not in the section 89 schemes. These services have their own terms and conditions which set out their individual compensation or reimbursement arrangements. Royal Mail also provides compensation for failure to obtain proof of delivery for Recorded Signed For (where the proof of delivery services has been paid for) and Special Delivery services.

## A requirement to provide reasonable (retail) compensation for universal services

- 6.44 We consider that we should retain the regulatory requirements on Royal Mail to provide retail compensation for loss, damage and delay for universal services where compensation is currently provided. We also consider that Royal Mail should continue to provide compensation if there are failures to the Redirections and Keepsafe services and where there has been a failure to obtain proof of delivery for Recorded Signed For and Special Delivery Next Day services.
- 6.45 This is because these universal services are used by residential customers and small business customers who have no realistic alternatives to Royal Mail, and the sums

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<sup>83</sup>

<http://www.royalmail.com/sites/default/files/docs/pdf/Redirections%20Social%20December%2010.pdf>

<sup>84</sup>[http://www.royalmail.com/sites/default/files/keepsafe\\_agreement.pdf](http://www.royalmail.com/sites/default/files/keepsafe_agreement.pdf)

involved in the conveyance of single piece post, and for Redirections and Keepsafe services, are for the most part so small that it is unrealistic to expect that customers would find legal action an effective remedy. In addition, proof of delivery has been identified as one of the key characteristics in the provision of relevant universal services in DUSP 1.4.

- 6.46 We consider that these customers should continue to be protected by way of compensation payable when postal packets are lost, damaged or delayed and where there are failures to the Redirections and Keepsafe services. The current retail compensation arrangements will be a direct protection for customers should Royal Mail's QoS be poor<sup>85</sup>.
- 6.47 In 2008 the requirement for Royal Mail to provide the bulk compensation scheme for delay was removed from the Direction made by Postcomm. In 2010, Postcomm also made a decision to remove bulk mail from the universal service. In light of this, we propose that there should be no regulatory requirements on Royal Mail to provide compensation for non-universal services. However, Royal Mail may voluntarily provide compensation or reimbursement for non-universal service products, as it currently does. Similarly we do not believe we need to mandate a requirement for reimbursement or compensation for all RPOs at this stage.
- 6.48 We also believe this requirement (in CP1) for Royal Mail to provide compensation for those universal services (for which it is currently provided) should - in line with our proposed approach to the non-price terms of universal services discussed in Section 5 – require that the compensation provided, is fair and reasonable. As a consequence of this, the review and modification provisions for any changes to Royal Mail's compensation arrangements for delay, currently in CP1, will fall away.

#### Reporting on compensation and our proposed amendment

- 6.49 Royal Mail's annual report on the operation of its compensation schemes must set out the number of complaints received incorporating the number of claims for compensation made and the amount of compensation paid. The report is broken down by the ten main causes of the claims. The reports show that loss, damage and delay are always in the top ten main causes of claims<sup>86</sup>.
- 6.50 As Ofcom will continue to require Royal Mail to provide compensation for loss, damage and delay to universal services currently covered by the relevant compensation arrangements, we consider that the current reporting requirements for the compensation arrangements should also stay the same, with *two exceptions*.
- 6.51 We propose to remove two elements of the current annual reporting requirements on Royal Mail.
- 6.52 Currently, in its annual report, Royal Mail must provide data for both the United Kingdom as a whole and also for each postcode area. The annual report must also include a statement of action that Royal Mail intends to take in the following year to address the causes of claims for compensation.

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<sup>85</sup>An increasingly important protection given the proposed lifting of the price controls and the cessation of the C factor quality of service incentive mechanism.

<sup>86</sup>[http://www.royalmailgroup.com/sites/default/files/docs/files/annex\\_a\\_national\\_summary\\_2010-11.pdf](http://www.royalmailgroup.com/sites/default/files/docs/files/annex_a_national_summary_2010-11.pdf)

- 6.53 Firstly, we propose to remove the reporting requirement for each postcode area for the following reasons:
- a) Ofcom has information gathering powers should information be needed on Royal Mail performance on a case by case basis.
  - b) The postcode area level information in the postcode area report does not provide meaningful comparative information about the relative performance of postcode areas. This is because it is often impossible to correctly identify the exact location of the issue as most users do not use tracked postal services. For example, in 2010/11 about 13% of all complaints could not be allocated to a postcode area at all – either because information was not available, or because they were international items. Such complaints still need to be allocated and therefore most complaints are generally allocated to the delivery office based on where the item was due to be delivered even though this may not be accurate. Also the data in the report only covers the number of complaints received and therefore any comparison of one postcode area with another postcode area's complaint levels will take no account of the respective mail volumes which can vary significantly between different postcode areas.
- 6.54 Secondly, we propose to remove the requirement to include statement of action that Royal Mail intends to take in the following year to address the causes of claims for compensation for the following reasons:
- a) As mentioned above, loss, damage and delay are likely to be the main causes for compensation claims. Most of the actions to address the causes of claims would already be covered in the action plan required under the Mail Integrity code of practice (condition E 1); and
  - b) We would still receive the annual complaint and compensation figures. And we have information gathering powers should information be needed on Royal Mail performance if we became concerned with an increase in complaint levels.
- 6.55 In light of the above, we believe that the report at postcode area level should be removed from the annual report as it provides no meaningful consumer protection or helpful consumer information about relative performance of postcode areas but does place an unnecessary regulatory burden on Royal Mail. Alternatively it may be appropriate for the current method of reporting to be amended to make it more useful to customers and Ofcom. However, the changes required to achieve this might be disproportionately onerous on Royal Mail and deliver minimal benefits to customers and Ofcom. We also consider that we should remove the requirement for Royal Mail to include a statement of action to address the causes of claims for compensation because loss, damage and delay are covered elsewhere.
- 6.56 Also, as noted in our discussion of consumer protection conditions 7-9 later on in this Section, we intend to conduct a review of complaints handling and redress. We would welcome feedback from stakeholders on any evidence on changes to reporting which could be made in the future as it would be useful to take account of any evidence stakeholders may have for that subsequent review.

#### Impact of our proposals for compensation arrangements

- 6.57 Senders and recipients of universal services currently covered by the existing compensation arrangements would continue to be able to claim compensation for loss, damage and delay for single piece items for any failures to the Redirections and



Keepsafe services and for failure to obtain proof of delivery for Recorded Signed For and Special Delivery next day services. There would also be regulatory certainty for Royal Mail as the consumer protection condition will make clear that Royal Mail is required to maintain compensation arrangements for relevant universal services. Whilst Royal Mail will have commercial freedom as to the details of the compensation arrangements, we would also expect that Royal Mail would be working closely with its customers to ensure that the terms and conditions for any changes to its compensation arrangements are fair and reasonable and we can investigate, in the unlikely event that this does not happen.

- 6.58 Royal Mail would continue to publish annual reports on the operation of its compensation schemes at a United Kingdom level. However the regulatory burden on Royal Mail would be lessened if we removed the postcode area level report and the statement of action to address the causes of claims for compensation in the following year. Because the area report does not provide meaningful comparative information about the relative performance of postcode areas, we do not consider that it provides any meaningful protection to users in the different parts of the UK or to users living respectively in urban and rural areas.

### **Summary of proposals on Royal Mail's compensation arrangements**

- 6.59 In light of the above, we propose to amend CP 1.12-17 and CP 2 to create one CP condition relating to compensation.
- 6.60 We propose that the compensation provided by the USP (Royal Mail) should be fair and reasonable in relation to relevant<sup>87</sup> services provided as part of the universal service. This means that the review and modification provisions for any changes to Royal Mail's compensation arrangements for delay (currently in CP 1) will fall away.
- 6.61 We also propose to remove the postcode area level element of the annual report currently required by CP 1.16.
- 6.62 We also propose to remove the requirement on Royal Mail to include a statement of action to address the causes of claims for compensation currently in CP1.16.

*Q6.2 Do you agree with our proposed requirement for Royal Mail's compensation arrangements for universal services? If not, please explain why.*

### **Measuring and reporting on quality standards by other RPOs**

- 6.63 Consumer protection condition 3 (previously condition 2 of the standard licence) requires a RPO other than Royal Mail to establish, within three months of starting conveyance of letters, adequate systems for measuring and recording its performance in achieving its contract targets. [We discussed our approach to quality standards and reporting for Royal Mail's universal and non-universal services in the previous Section where we proposed to remove targets and reporting for Royal Mail's non-universal services].
- 6.64 In addition, such RPOs must provide Ofcom and with an annual report in relation to their performance in achieving their contract targets. Ofcom and Consumer Focus may publish these reports after notifying the RPO.

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<sup>87</sup> Certain services in the universal service are provided free of charge – therefore it would not be relevant for Royal Mail to pay compensation in relation to such services.

- 6.65 The condition only applies to contract targets. Contract targets are defined as; “Such targets for obligations in respect of service performance as are set out in the RPOs contracts with its customers”. Therefore, this regulatory condition only applies to customers who have a contract with an RPO. Most customers using RPOs other than Royal Mail are business customers or those sending higher mail volumes.
- 6.66 The Mail Competition Forum (MCF) in their response to the August consultation on the transition to new regulatory framework<sup>88</sup> suggested that these requirements could be removed as they “provided no meaningful consumer protection”. The MCF felt that “performance targets were largely bespoke and often not guaranteed so measurement was very difficult” and that “comparison of disparate standards was also of little use”.

### Information is important to the development of competition

- 6.67 Postcomm brought in these requirements in 2005. In its decision document Postcomm set out<sup>89</sup> that the availability of information to customers and potential customers was essential to the development of effective competition. Postcomm also stated that such regulatory requirements were needed to ensure that customers could be informed about the performance of licensees. However, after these requirements were introduced, neither Postcomm nor Consumer Focus published the annual reports.
- 6.68 In order to monitor the development of competition, Postcomm carried out annual business customer surveys. One aspect of the surveys was to monitor awareness, use and satisfaction with RPOs and Royal Mail. In 2009, the survey noted that those business customers using RPOs other than Royal Mail, gave a satisfaction score of 7.9 out of 10<sup>90</sup>. Royal Mail scored an average of 7.8 out of 10.
- 6.69 In 2010, Postcomm commissioned a retail market survey<sup>91</sup> which showed that smaller business mailers<sup>92</sup> were aware of RPOs other than Royal Mail, 11% had used an RPO other than Royal Mail in the last three years and of those only 1% had switched back to Royal Mail. For larger business mailers<sup>93</sup> one in six were using an RPO other than Royal Mail. Of those who had not moved away from Royal Mail, one of the reasons for not switching was concern about potentially lower service quality. Where mailers had switched away from Royal Mail, they were usually happy with the results of the switch.

### Competitive drivers can help sustain service levels

- 6.70 Since these regulatory requirements were put in place by Postcomm, competition has developed in several areas of the postal market. Market forces tend to help drive required service levels and it is clear from Postcomm’s survey results that customers

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<sup>88</sup> The MCF response can be found here:

[http://stakeholders.ofcom.org.uk/binaries/consultations/postal-regulation/responses/Mail\\_Competition\\_Forum.pdf](http://stakeholders.ofcom.org.uk/binaries/consultations/postal-regulation/responses/Mail_Competition_Forum.pdf)

<sup>89</sup> Postcomm, August 2005, Decision document “Licences under the Postal Services Act 2000: Licensing framework in a fully open market”.

<sup>90</sup> Postcomm, 2009 Business Customer Survey Summary.

<sup>91</sup> Postcomm, December 2010, Postcomm retail market survey 2010, <http://stakeholders.ofcom.org.uk/binaries/post/1810.pdf>

<sup>92</sup> Defined as those spending £5,000 or less a year on postage.

<sup>93</sup> Defined as those spending £50,000 or more a year on postage.

need assurance about service quality. It is therefore in the interest of the RPO to voluntarily measure and record its performance against its contract targets without regulatory intervention. RPOs also need to provide information to customers on performance against contract targets in order to win and retain customers. In the event a customer becomes dissatisfied with the RPO's performance against its contract targets, it can choose to switch to another RPO.

### **We propose that the requirement for other RPOs to measure and report on quality standards is no longer required**

- 6.71 In light of the above, we believe it is likely that market forces should provide the desired levels of service for contract customers and that contractual arrangements would already be in place to ensure operators provide the required information. We believe RPOs have an incentive to measure and record and provide information to customers on performance against contract targets regardless of there being a regulatory requirement in place.
- 6.72 We also consider that our reasoning for removing reporting requirements on Royal Mail in relation to non-universal service products (CP 1 – discussed in the previous Section) applies equally to services provided by other RPOs. Removing the requirement would maintain a level playing field.
- 6.73 Therefore, we propose to delete CP 3 in its entirety.

#### Impacts of our proposal

- 6.74 We believe the impact on consumers of removing the requirements is likely to be minimal as market forces should ensure RPOs measure and provide to customers their contract target performance. As the annual reports were never published by Postcomm or Consumer Focus, we believe removing the obligation to produce them would have no impact on users in terms of the availability of information about performance.
- 6.75 Removing this condition may have a small positive impact on RPOs in that it would reduce compliance costs.
- 6.76 We believe we can also mitigate any impacts from removing this regulatory condition as we
- intend to carry out regular market research in relation to business mailers which will help us to monitor awareness, use and satisfaction with RPOs and Royal Mail; and
  - both Ofcom and Consumer Focus have information gathering powers should information be needed on RPO performance.

*Q6.3 Do you agree with our proposal to remove CP 3 which requires other RPOs to measure and report on their contract targets? If not, please explain why.*

### **Common operational procedures**

- 6.77 CP 5 (previously condition 14 of Royal Mail's licence and condition 4 of the standard licence) requires RPOs to comply with the Postal Common Operational Procedures

Code<sup>94</sup>. The Code is intended to minimise the risk of mis-posted, mis-collected or mis-directed postal packets not being repatriated to the correct RPO, customer or addressee and covers the handling of misdirected or mis-collected letters as well as misdirected complaints and enquiries.

- 6.78 CP 5 requires RPOs to become party to a Postal Common Operational Procedures Agreement (PCOPA<sup>95</sup>) which is referenced in CP 5 and to comply with a Postal Common Operational Procedures Code (PCOPC) which is Annexed to CP 5 itself. This is to ensure they make collective arrangements and also comply with certain procedures covering the handling of misdirected or mis-collected letters, as well as misdirected complaints and enquiries.
- 6.79 Apart from the proposed changes (i.e. extending the Code to all access operators and expanding the scope of postal packets to which the Code applies) that we set out earlier in this Section - as part our discussion on CP 1.2(b) – as well as any other amendments consequential to those changes, we do not propose any other changes to CP 5 or the PCOPC as we feel it is still necessary to ensure that such arrangements are in place (and complied with) so that consumers can receive misdirected/mis-collected letters and have their complaints or enquiries dealt with appropriately.
- 6.80 However, during our initial conditions review, a few stakeholders suggested changes could be made to the PCOPA. Subsequently, two parties to the PCOPA – Royal Mail and TNT - submitted requests to us earlier this month in the required format (as specified in clause CP 5.5(b) and set out in clause PCOPA 12.5), proposing a number of amendments.

### **We will be consulting shortly on proposed amendments to the PCOPA which is referenced in CP 5**

- 6.81 We have considered these requests in line with what is required of us under CP 5.5 i.e. whether we believe they will enable the Code Objectives to be better fulfilled and whether such modifications are consistent with our statutory duties.
- 6.82 We intend to consult (separately) on them, very shortly. We will do this by issuing a formal Notice of modification of the “Postal Common Operational Procedures Agreement”, in order to fulfil CP 5.7(b). We will also directly notify parties to the PCOPA as well as Consumer Focus in line with the requirement on us at CP 5.7(a).
- 6.83 Subject to consultation responses, we would intend to make appropriate changes to the PCOPA (via a direction) along with our eventual statement on the regulatory conditions.

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<sup>94</sup> Operators must comply with such a Code *unless* Ofcom otherwise consents. The Code applies in so far it is consistent with or deals with matters not provided for by any Access agreement to which the operator is party - or unless the operator has established alternative arrangements with other regulated postal operators relating to the treatment of mis-directed, mis-posted and mis-collected mail.

<sup>95</sup>

<http://webarchive.nationalarchives.gov.uk/20111027102050/http://www.psc.gov.uk/documents/2067.pdf>

## Contributions to consumer bodies' expenses

- 6.84 This consumer protection condition 6, (previously licence condition 20 of Royal Mail's licence and condition 10 of the standard licence), sets out how consumer bodies' expenses will be allocated and recovered from RPOs.
- 6.85 The condition sets out that RPOs with a turnover for regulated postal services of at least £10M must contribute towards the qualifying consumer expenses of Consumer Focus and the OFT. For the OFT only those expenses relating to the expansion of the Consumer Direct service which caters for postal service customers qualify.
- 6.86 The condition also sets out that all RPOs, regardless of regulated turnover, must contribute appropriately for any directly attributable costs in relation to the qualifying consumer expenses of the OFT which relate to the Consumer Direct service (excluding expansion costs) which caters for postal service customers.
- 6.87 The only change we propose to make to this condition is to remove CP 6.5 which relates to any requests of payments made by Postcomm or payments made to Postcomm. This provision is no longer required as all requests for payments and all payments will now be made by/to Ofcom.
- 6.88 We do not propose any other to this condition at this stage. However, we note that from April 2012, Citizens Advice will provide a telephone and online consumer advice service in place of Consumer Direct. In light of this change in provider, we will need to change the references to the OFT and Consumer Direct. However, we cannot do this unless the Postal Service Act 2011 is amended as currently we can only recover consumer body expenses in relation to Consumer Focus or the OFT.

## Consumer complaints handling and redress

- 6.89 There are currently three consumer protection conditions (7-9) which relate to handling consumer complaints and membership of redress schemes:
- **CP 7** which requires any postal operator to set up and adhere to transparent, simple and inexpensive procedures for dealing with complaints from consumers of postal services. The procedures must facilitate the fair and quick settlement of disputes;
  - **CP 8** which sets out further requirements in relation to complaint handling specifically for RPOs providing regulated postal services. For example requiring the publication of an annual consumer complaints report; and
  - **CP 9** which requires an RPO providing regulated postal services to be a member of a qualifying redress scheme. Currently POSTRS<sup>96</sup> is the only qualifying redress scheme in place.
- 6.90 Under the transitional provisions set out in Schedule 9 of the Act, Ofcom was required to determine the regulatory conditions under the new general authorisation regime to apply with effect from 1 October 2011. Regulatory conditions CP 7 – 9 were created as part of this process. Previously, the provisions of CP 8 and 9 sat outside of the licence conditions as the Consumers, Estate Agents and Redress Act 2007 ("CEARA") required Postcomm to make regulations in relation to complaint

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<sup>96</sup> The Postal Redress Service - <http://www.postrs.org.uk/> .

handling and allowed the Secretary of State to make an order requiring certain postal operators to be members of an approved redress scheme.

- 6.91 Ofcom brought the requirements set out in the Postal Services (Consumer Complaint Handling Standards) Regulations 2008 and the requirement to be a member of an approved redress scheme into the consumer protection conditions as allowed for under the Act. Ofcom also brought in the requirement in the Directive for all postal operators to set up and adhere to transparent, simple and inexpensive procedures for dealing with complaints from consumers of postal services.
- 6.92 Three conditions were created during this process to make it clear to stakeholders how the separate provisions of the Directive, redress requirement and the Postal Services (Consumer Complaint Handling Standards) Regulations 2008<sup>97</sup> had been transposed into the regulatory conditions.

### **We plan to merge the conditions, correct an error in transposition and change the reference to Consumer Direct to Citizens Advice Consumer Service**

- 6.93 As we move forward into the new authorisation regime, we feel it is now sensible to consolidate these requirements into one complaint handling and redress condition. This will make it easier for stakeholders now and in the future to understand the complaint handling and redress requirements which are in place.
- 6.94 However, in the course of reviewing these conditions we identified a transposition error, the effect of which was that postal packets other than letters, conveyed in the provision of the universal service, were no longer covered by CP 8 and 9. We propose to correct this by specifying in CP 8 and 9 where postal packets other than letters, are conveyed in the provision of the universal service. Annex 11 sets out this proposal.
- 6.95 We also need to update the reference to Consumer Direct in CP 8.2(i) as from April 2012 Citizens Advice will provide a telephone and online consumer advice service in place of Consumer Direct. In light of this change in provider, we need to change the reference in CP 8.2(i), and the associated definition, from 'Consumer Direct' to 'Citizens Advice Consumer Service'.

### **A wider review of complaints handling and redress will be conducted later**

- 6.96 At this stage, we do not intend to make any changes to the conditions other than those stated above.
- 6.97 However, we would welcome feedback from stakeholders on any evidence relating to changes which could be made in the future. In the August consultation on the transition to the new regulatory regime<sup>98</sup>, we stated we would provide further information about the scope and timing of our proposed review of complaints-handling and redress, and seek views from stakeholders, as part of our annual planning process and it would be useful to feed in any evidence stakeholders may have into that review.

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<sup>97</sup> These regulations can be found here: <http://www.legislation.gov.uk/ukxi/2008/2355/contents/made>

<sup>98</sup> Ofcom, *Postal Regulation: transition to the new regulatory framework, a consultation* 8 August 2011, <http://stakeholders.ofcom.org.uk/consultations/postal-regulation/>

- 6.98 As we are only proposing to merge the conditions, correct an error to re-establish the regulatory regime as it applied before 1 October 2011, and ensure the condition refers to the correct provider of a consumer advice line we consider the likely impact on postal operators and consumers to be negligible.
- 6.99 RPOs will need to update their complaints handling procedure to ensure it refers to the correct consumer advice provider. However, this should only impose minimal impacts on RPOs' online procedures. We acknowledge that there will be some impact for those RPOs who have printed literature which refers to Consumer Direct. However, as Citizens Advice will continue to use the Consumer Direct telephone number, RPOs can gradually phase out any printed literature which refers to Consumer Direct over the next six months.

### **Consumer complaints handling by the designated universal service provider**

- 6.100 Condition DUSP 6 (formerly condition 5 of Royal Mail's licence) requires Royal Mail to publish and provide to Ofcom and Consumer Focus quarterly reports on the number of consumer complaints received and completed.
- 6.101 This condition relates to the work carried out by Postcomm in 2008 when it brought in the new complaint handling and redress arrangements required by the Consumers, Estate Agents and Redress Act 2007. In its decision document, Postcomm said that quarterly reporting was required for Royal Mail as it provided the universal service and was the dominant provider in the licensed postal sector and was therefore likely to be subject to a greater volume of complaints than other licensed postal operators. This decision reflected feedback from consultation responses which commented that annual reporting was too late to identify performance failures and as the universal service provider, Royal Mail should have more frequent reporting requirements.

### **Incorporating this requirement in the CP consumer complaints condition**

- 6.102 While this is currently a DUSP, the condition is linked to CP 8.14 and CP 8.15 which require RPOs to publish an annual consumer complaints report setting out the number of complaints received and the number resolved each year. DUSP 6 places an additional reporting requirement on Royal Mail, as the universal service provider, to provide quarterly reports in addition to the annual reports required of all RPOs.
- 6.103 Therefore we propose to include this requirement within the (proposed) merged consumer protection conditions on consumer complaints and redress. It should provide more regulatory clarity to put all these requirements within one condition.
- 6.104 While we do not propose to make any substantive changes to the condition at present, we would still welcome feedback from stakeholders on whether quarterly reporting is still required, as it would be useful to feed in any evidence that stakeholders may have into proposed review of complaints-handling and redress mentioned further above.

### **Summary of our proposals on CP 7-9 and DUSP 6**

- 6.105 We propose to correct the transposition error as shown in Annex 11.
- 6.106 We propose to replace the reference to "Consumer Direct" in CP 8.2(i) with "the Citizens Advice consumer service". The "Citizens Advice consumer service" will be

defined as “the telephone and online consumer advice service operated by Citizens Advice”.

- 6.107 We propose to merge these three CP (7-9) conditions with the quarterly reporting requirement on Royal Mail (under DUSP 6) into one condition.

## **The Essential Condition on Mail Integrity**

- 6.108 Essential condition E 1 (previously condition 8 of Royal Mail’s licence and condition 3 of the standard licence) requires all RPOs to comply with the Mail Integrity Code of Practice, the purpose of which is to minimise the exposure of Code Postal Packets to the risk of loss, theft, damage and/or interference; and maintain and improve their performance in this regard.
- 6.109 The Mail Integrity Code was introduced in 2006 and established minimum common standards for mail integrity for all authorised postal operators. It facilitated consumer understanding of what users of postal services could expect from a postal operator in terms of security of mail entrusted to them. Without such a common requirement across postal operators, there may be a risk that consumers lose confidence in the postal system as there could be less consistency in the levels of security afforded to their mail when conveyed across the postal delivery chain.
- 6.110 Apart from the proposed changes we set out earlier in this Section – as part our discussion on CP 1.2(b) – we do not propose any other substantive changes to E 1 or the Mail Integrity Code as we feel it is still necessary to ensure that such arrangements are in place (and complied with). The draft condition is in Annex 16.

## **Summary of proposed changes to consumer protection conditions<sup>99</sup> and the essential condition**

- 6.111 We propose:
- a) To remove the regulatory requirement on RPOs – at CP 1.2 – to use reasonable endeavours to collect postal packets, as agreed with their customers and deliver them appropriately within a reasonable time (and make related amendments to the Postal Common Operational Procedures Code and Mail Integrity Code);
  - b) To create a requirement which requires Royal Mail to provide reasonable compensation for loss, damage or delay to customers of universal services (for the services which Royal Mail currently provides compensation);
  - c) To remove the obligation on other RPOs (i.e. not Royal Mail) relating to them measuring and reporting on their contract targets;
  - d) Merge consumer complaints and redress conditions for postal operators and Royal Mail into one condition, make a minor correction to the newly merged consumer complaints and redress condition which apply to postal operators generally (as well as changing references from Consumer Direct to Citizens Advice); and
  - e) Make a minor correction to the essential condition on mail integrity, which applies to all RPOs.

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<sup>99</sup> The draft consumer protection conditions are in Annex 11.



## Tests for imposing consumer protection conditions

6.112 We now discuss the legal tests for (a) to (c) noted above. We consider the explanation above to be a sufficient demonstration that the test is met for (d) and (e).

6.113 We believe the changes to CP 1 to remove the requirement on RPOs (in relation to regulated postal services) to use reasonable endeavours to collect postal packets as agreed with their customers and to deliver them appropriately (and the related changes to the PCOPC and Mail Integrity code) are:

- **Objectively justifiable** because contractual remedies and market forces should provide the desired levels of collections and delivery service for customers in the absence of a regulatory requirement. Also, the related amendments to the PCOPC and Mail Integrity code are necessary to ensure any postal packet sent via Royal Mail, an RPO or an Access Operator are covered by the mis-directed, mis-posted or mis-collected provisions as well as mail integrity provisions. As we have discussed above, in a multi-operator environment where customers use more than one operator there is scope for mistakes to arise. Access operators carry approximately 40% of mail, and as they are handling mail it is appropriate to require such operators to be subject to the requirements of the Codes;
- **Not unduly discriminatory** the change to CP1.2 would apply to all RPOs equally and the changes to the PCOPC and Mail Integrity code also bring more consistency to their application across operators who are handling mail in a multi-operator environment;
- **Proportionate** because if the market can reasonably be expected to meet customers' needs it would not be proportionate to impose the requirement at CP 1.2. We believe that the changes to the PCOPC and Mail Integrity code are proportionate to ensure those handling mail in a multi-operator environment are subject to the same procedures. The proposed changes will provide consumer benefits and extending the Codes to access operators does not impose a disproportionate burden on such operators since the Codes currently apply to all regulated postal operators, many of whom are sole traders with significantly smaller businesses than access operators and the requirement to comply with these Codes has not prevented the development of smaller regulated postal operators. Furthermore, the changes go no further than is necessary to ensure the benefits outlined above can be achieved; and
- **Transparent** because it is clear that the changes are intended to remove an unnecessary requirement (CP 1.2) and make necessary related changes to industry codes.

6.114 We believe the proposed requirement for compensation arrangements for universal services is:

- **Objectively justifiable** because compensation is warranted for universal services which are predominantly used by residential customers and small business and these customers need to be protected by way of compensation payable when postal packets are lost, damaged or delayed since they are too small by themselves to be able to negotiate with the USP;
- **Not unduly discriminatory** because the change necessarily affects the USP – and there is only one such USP (Royal Mail) in the UK;

- **Proportionate** because we need to protect senders and recipients of universal services (in relation to compensation for loss, damage and delay), we are only requiring compensation for those universal services for which it is currently provided and because we need to ensure compensation is retained for all those services (given they are mainly used by residential customers and small business customers who have no realistic alternatives to Royal Mail or who are unlikely to find legal action an effective remedy); and
- **Transparent** because it is clear that the change is intended to provide regulatory certainty in terms of compensation requirements for universal services.

6.115 We believe deletion of requirements on other RPOs to measure and report on their contract targets is:

- **Objectively justifiable** because competitive drivers should encourage these operators to maintain, monitor and record QoS absent a regulatory requirement;
- **Not unduly discriminatory** because it will apply to RPOs other than Royal Mail and would also be in line with our approach to remove targets (and reporting on these) for Royal Mail's non-universal services;
- **Proportionate** because the market can reasonably be expected to meet customers' needs – and so it would not be proportionate to impose this regulation; and
- **Transparent** because it is clear that the change is intended to remove an unnecessary requirement.

## Section 7

# End-to-end competitive entry notification process

## Background

7.1 Section 41 of the Act gives Ofcom a power to impose a notification condition on every person providing or intending to provide a service within the scope of the universal postal service. Such a condition could require such persons to provide advance notice of their intention either (i) to provide a letters business on a specified scale (whether or not the person is currently providing a letters business or any other postal service), or (ii) where the person is already providing a letters business on a specified scale, advance notice of the person's intention to expand the business by a specified extent.

7.2 In April 2011, the Secretary of State for Business, Innovation and Skills wrote to Colette Bowe, the chair of Ofcom, and Millie Banerjee, the chair of Postcomm. This was in the context of the Government's publication of a package of amendments to the Postal Services Bill. In this letter, the Secretary of State stated:

"If approved by Parliament, there would be a new power for Ofcom that would allow them to require anyone seeking to set up (or expand) a significant letter delivery service to notify Ofcom before commencing operations. This would give Ofcom the time to consider whether any regulatory conditions needed to be imposed on the operator in order to prevent any "cherry-picking" that would undermine the universal postal service"<sup>100</sup>.

7.3 On 1 October 2011 the Secretary of State issued such a direction to us, giving us six months to set this condition in place<sup>9</sup>.

7.4 Implicit in the Act is that a notification of end-to-end entry will allow Ofcom to consider whether the proposed entry is likely to harm the universal service. If we thought this to be the case we could then consider imposing regulatory conditions in order to secure ongoing provision of the universal postal service, such as a General Universal Service Condition under section 42 of the Act which could contain "such obligations as OFCOM consider necessary to impose for, or in connection with, securing the provision of a universal postal service in accordance with the standards set out in the universal postal service order."

7.5 In the October consultation, with regard to end-to-end competition, we proposed the following:

"As we have set out above it is clearly possible to hypothesise forms of end-to-end competition that could have a net benefit to the universal service. For example, entry on an efficient basis and at a reasonable scale might be expected to have this effect. However, it is also possible to hypothesise forms of end-to-end competition that

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<sup>100</sup><http://www.bis.gov.uk/assets/biscore/business-sectors/docs/p/11-874-postal-regulatory-framework-letter-to-ofcom-postcomm>

would have a detrimental effect on the universal service. For example, Royal Mail's Universal Service Obligation may result in competition entering that is based on an arbitrage opportunity (i.e. competition that is based on Royal Mail's price inflexibility due to its universal service obligation rather than due to underlying efficiency advantages), leaving Royal Mail to bear the cost of the most expensive areas and at such a pace and volume that Royal Mail is unable to respond.

As noted above we will implement the notification condition by 31 March 2012 as directed by the Secretary of State. We will assess any potential entry or growth notified to us under this condition on a case-by-case basis to determine whether we should consider taking any regulatory steps to secure our duties under the Act.

Meanwhile, in the event that we become aware that a postal operator is planning to enter the end-to-end market in such a way as would have triggered a likely notification condition, we will carry out the same assessment against our duties".<sup>101</sup>

## **Our proposed notification condition on end-to-end entry or expansion**

- 7.6 The key objectives in setting the thresholds for a notification requirement are that they are simple to implement and understand, must be capable of being predicted relatively easily by the new entrant, ensure that we are informed of any significant entry or growth, but not lead to us being inundated with notifications about insignificant plans.
- 7.7 Therefore, we propose to require three months' advance notification to Ofcom if the relevant person is planning:
- i) to enter the market and deliver more than 2.5 million letters anywhere in the UK in the quarter following the notification period; or
  - ii) to increase the volume of letters it is carrying by more than 2.5 million in the quarter following the notification period.
- 7.8 We consider these thresholds are consistent with securing the provision of the universal service, as they are well below the level where Royal Mail would be losing any significant volume. 10 million letters per year is less than 0.1% of Royal Mail's letters volumes. The thresholds are also significantly higher than the current level of end-to-end competition. In the last 12 months less than 10 million letters were delivered by end-to-end by competitors to Royal Mail.
- 7.9 We consider that three months is an appropriate advance notification period as it is long enough to allow us some time to understand the operator's plan before it is implemented but short enough so that it clearly falls within a reasonable planning horizon for the operator.

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<sup>101</sup> Paragraphs 7.25-7.27 of <http://stakeholders.ofcom.org.uk/binaries/consultations/securing-the-postal-service/summary/condoc.pdf>

- 7.10 The condition will also set out the basic set of information that affected persons should set out to us. We propose that a notifying postal operator (or potential postal operator) should in the first instance provide the following information:
- Their name and address;
  - The total volume of letters they forecast they will deliver in the quarter following the notification period;
  - In what areas they are planning to deliver and the forecasted volumes of delivered letters in each of these areas; and
  - If they are notifying their intention to start operations, the date at which they plan to start delivering in each of these areas.

*Q7.1: Do you agree with the thresholds, timescales and content of notifications under the proposed condition? If not, please provide your reasons.*

## Process for notifications

- 7.11 As noted above we have set out that we intend to assess any potential entry or growth notified to us under this condition on a case-by-case basis to determine whether we should consider taking any regulatory steps to secure provision of the universal service in accordance with our duties under the Act. However, in the interests of clarity and certainty, below we set out the process we expect to follow.
- 7.12 Ofcom will acknowledge the receipt of any notification within five working days. At this time or shortly thereafter Ofcom may request further information on the proposals contained in the notification. We may also collect information from other postal operators or relevant parties.
- 7.13 Within a month of receipt of a notification, Ofcom will indicate to the notifying person/postal operator whether or not we consider further analysis is necessary. If we believe further analysis is necessary we will set out a likely timetable to the notifying person/postal operator at this time. However, the end-to-end notification condition is not an approval process. It does not prevent a person/postal operator from providing services; it only requires the person/postal operator to notify Ofcom in advance.
- 7.14 If following our analysis we consider that we should impose any regulatory conditions in order to secure the provision of the universal postal service, we will consult on any such condition for a period of at least one month. This will allow all interested parties the ability to comment on our proposals before they are implemented.

## Confidentiality of the process

- 7.15 The Act has strict provisions regarding confidentiality of information. Section 56 of the Act regarding the treatment of information obtained under Part 3 of the Act allows disclosure by Ofcom only in specified circumstances, contravention of which is an offence. Section 56(2)(b) permits Ofcom to disclose information where it is necessary for the purpose of facilitating the carrying out by Ofcom of its statutory functions.
- 7.16 It may also be the case that some information provided to Ofcom under the notification condition will be commercially sensitive information, the disclosure of

which might risk compromising the notifying operator's legitimate commercial interests and/or might not be compatible with competition law principles.

- 7.17 We will consider on a case by case basis whether and/or to what extent, we should publish the disclosure of information provided to Ofcom under a notification condition, in advance of any consultation on the imposition of any regulatory condition as a result of the notification.

*Q7.2: Do you agree with Ofcom's proposed process for handling end-to-end notifications? If not please provide your reasons.*

### Impacts

- 7.18 In terms of impact, we note no direct consequences necessarily follow a notification. The notification condition is essentially required for our own analytical purposes i.e. so that we are alerted to either end-to-end entry or growth into a competing letters delivery service and can therefore use that information to understand the impact of such a development on the provision of universal service.

## Summary of our proposals

- 7.19 We propose a new notification condition – available at Annex 15 – as set out above so we can assess any impacts on universal service provision, from plans by other postal operators seeking to offer or expand an end-to-end competing (letters) delivery service.
- 7.20 We believe this notification condition is:
- **Objectively justifiable** because we have been directed to put in place a condition to cover this notification process, and the levels we propose should trigger the notification requirement are intended to be high enough to avoid the notification of immaterial entry/expansion, but low enough to cover entry/expansion of a scale that, whilst higher than any existing letter delivery operations in the market, is not likely to be immaterial;
  - **Not unduly discriminatory** because it will apply to any operator who plans to enter or expand their business (providing a letters delivery service) above specified thresholds;
  - **Proportionate** because the thresholds are set a level which we consider strikes an appropriate balance between the need for us to be notified of material entry whilst not imposing an undue burden on persons/operators; and
  - **Transparent** because it is clear why this notification is required – that is, to allow us to assess the potential impact of such entry or expansion on universal services.

## Section 8

# Implementing our proposal for a safeguard cap for Second Class stamps

## A price cap for Second Class stamps

- 8.1 In the October consultation, we proposed to grant Royal Mail commercial freedom for a period of seven years by not imposing a traditional price control subject to a number of safeguards.
- 8.2 One of those safeguards was to ensure that a basic universal service product is available to all and affordable to all. Therefore, in section 6 of our October consultation we proposed to set a safeguard cap for Second Class stamped (standard letters) only.
- 8.3 This would represent a new form of price control on Royal Mail, and should not be compared to the current price control obligations in T4 discussed in Section 11, which are for a different purpose and have a very different impact on Royal Mail's pricing and commercial flexibility.
- 8.4 That October consultation contained the reasons for and impact assessment of our policy proposals and we refer stakeholders to that consultation. In this Section, we are only discussing how we would implement a cap via a condition, if we ultimately decide to impose a safeguard cap on Second Class stamps once we have considered responses to both our October consultation and this consultation.

## Our proposal to implement the safeguard

- 8.5 The text of our proposed DUSP condition containing the safeguard cap is set out at Annex 10. We will decide on the appropriate numbering of this requirement/condition when we make our decisions in March 2012.
- 8.6 We propose that the formula for the cap will be:
  - a) In the first year (2012-13), the stamp price should be no more than x pence. We have indicated that the range for x will be between 45p and 55p.
  - b) In the following years, the cap will increase by RPI. To provide certainty for Royal Mail and customers, RPI should be measurable at the time Royal Mail provides its prices. We propose to use the full year average change in RPI from September to September, so that Royal Mail can set its prices using the most up to date data.
- 8.7 The cap will be a simple cap on any price charge for the basic weight step for Second Class stamps of 0-100g. If Royal Mail chooses to offer discounts to this price (for example, seasonal discounts, discounts for bulk purchase or electronic purchase) these will not impact the need to charge no more than the price cap for the basic service.
- 8.8 We have highlighted in the consultation that we are considering the need for other Second Class stamp services, including Large Letters and Packets, to be covered by a cap in order to protect vulnerable customers. If we were to conclude that a further

safeguard cap was required in relation to these formats and weight steps, then we would impose a second cap on those services, which would be a simple weighted average price cap for these higher weight services, which would also increase with inflation in a comparable manner. The form of the cap for the standard letter service would be unchanged.

- 8.9 We recognise that over a seven year period it is possible that the form of the basic weight step offered by Royal Mail could change. Other countries have different obligations on the weight or size of the letter for the basic weight step. If Royal Mail wanted to change the service offered, we would consider on a case-by-case basis whether a review of the level of the price cap would be appropriate. Unless any such review is undertaken, the cap would apply to the price of Second Class letters up to 100g.

## Legal tests

- 8.10 We set out, in paragraphs 9.7-9.19 of the October consultation, our analysis of the legal tests which we must meet in order to impose a DUSP condition such as this. As we are simply setting out how we would implement that earlier proposal to create a condition, we do not repeat that analysis here.
- 8.11 We were not able in the October consultation to address fully the requirement that any condition should be transparent, as we did not at the time publish the text of the proposed DUSP condition containing the safeguard price cap. We are now publishing that text for consultation as part of this document. We therefore consider that the proposed DUSP condition is transparent, not only because it is now published for consultation, but also because we consider that it is sufficiently clear from the text what the intended effect of the condition would be.

*Q8.1 Do you agree with our proposed drafting for the Second Class price cap DUSP Condition? If not, please provide your reasons.*



## Section 9

# Implementing our proposals for access

## Access obligations under initial conditions

9.1 Royal Mail is currently subject to four universal service provider access conditions that set out the basis on which it is required to provide access to its postal network to other operators. These are:

- **USPA 1** – this condition (licence condition 9 under the previous regulatory regime) requires Royal Mail to offer a statement on the terms on which it is prepared to offer access and to negotiate in good faith with applicants who seek access to its postal network. It also sets out a process for applicants to apply to Ofcom for a direction in the event that negotiations do not result in agreement with Royal Mail.
- **USPA 2** – this condition (previously licence condition 9) applies in the event that Royal Mail has established arrangements in relation to the use of its postal network through an ‘access code’. Where an access code is established, it requires Royal Mail to enter into arrangements with other requesting parties (for use of its postal network) if they conform to relevant provisions of the access code.
- **USPA 3** – this condition (previously licence condition 10) prohibits Royal Mail from obtaining any unfair commercial advantage in connection with the provision of access to its postal network.
- **USPA 4** – this condition (previously licence condition 21) sets out specific obligations in relation to the pricing of access services. First, the condition sets out the minimum level of margin that Royal Mail is required to maintain between the price of a set of access services and their equivalent retail services. Second, it imposes obligations around the pricing of ‘zonal access’ services.

## Proposed single USP access condition for access to IMC for purposes of providing D+2 and later than D+2 Letters and Large Letters service

9.2 We set out our proposals for regulating access in our October consultation (Section 7 and Annex 7). We are currently consulting on these proposals and recognise that responses to our proposals will need to be considered as part of the work in finalising the Regulatory Conditions for March 2012.

9.3 To implement the proposals outlined in our October consultation and summarised below we intend to replace the four initial conditions (USPA 1 – USPA 4 described above) with a single USP access condition setting out Royal Mail’s regulatory obligations in relation to offering access at the Inward Mail Centre (‘IMC’) for the purpose of providing D+2 and later than D+2 Letters and Large Letters services. We consider that establishing a single USP access condition that includes all of Royal Mail’s regulatory obligations for this form of access is in accordance with how the Postal Services Act envisages that a USP access condition should be imposed.

- 9.4 In the event that Ofcom concluded that Royal Mail should be obliged to offer access at any other points in its network, or to enable access users to participate in any additional markets requiring different points of access, we would expect these obligations to be imposed through establishing further USP access conditions.
- 9.5 In addition to the USP access condition, as part of our October consultation we have sought views on whether it is appropriate for Ofcom to provide guidance on specific issues in relation to access and have set out certain areas that we propose be included in that guidance.
- 9.6 In the event that guidance is provided, this is intended to supplement the USP access condition rather than being included as part of the USP access condition. It is our intention that such guidance would be published in March 2012 as a draft that would be subject to industry views before being finalised.
- 9.7 A summary of the proposals from our October consultation is provided below, together with an explanation of how we propose they should be reflected in the USP access condition, and how we envisage that the condition would be implemented in practice.
- 9.8 As part of this document we also provide proposals that supplement those set out in our October consultation. These supplementary proposals set out more detailed aspects of the implementation of the proposed new access framework.

### **Obligation on Royal Mail to offer access to the postal network – D+2 and later than D+2 Letters and Large Letter services**

- 9.9 The Act sets out three tests which must be satisfied in order for a Universal Service Provider to be required to give access to its network. Ofcom may not impose a condition requiring such access unless it appears to it that a condition is appropriate for each of the following purposes:
- Promoting efficiency;
  - Promoting effective competition; and
  - Conferring significant benefits on users.
- 9.10 In our October consultation (paragraphs 7.28-7.60), we considered that the tests in the Act were satisfied in relation to obliging Royal Mail to offer access for participation in the retail D+2 and later than D+2 Letters and Large Letters markets.
- 9.11 When deciding what obligations should be imposed in a USP access condition, the Act requires that Ofcom must in particular take into account five factors. The five factors are as follows:
- the technical and economic viability, having regard to the state of market development, of installing and using facilities that would make the proposed access unnecessary;
  - the feasibility of giving the proposed access;
  - the investment made by Royal Mail in relation to the matters in respect of which access is proposed;

- the need to secure effective competition in the long term; and
  - any rights to intellectual property that are relevant to the proposal.
- 9.12 In our October consultation, we considered that these five factors indicated that the appropriate point of access for participation in the relevant D+2 and later than D+2 Letters and Large Letters markets was at the IMC. In reaching this view we took into account Postcomm's preliminary assessment. This assessment recognised the fact that downstream access users currently inject items at this point shows that it is feasible (access at the IMC for participating in the D+2 and later than D+2 Letters and Large Letters market accounts for over 99% of access items). The assessment also identified various reasons why the Mail Centre network provides a suitable set of premises for such purposes.
- 9.13 The October consultation (paragraphs 7.61-7.64) proposed that access at the IMC for participating in the retail D+2 and later than D+2 Letters and Large Letters markets was consistent with Ofcom's primary duty to secure the provision of a universal postal service.
- 9.14 In requiring Royal Mail to offer access at the IMC for participation in the retail D+2 and later than D+2 Letters and Large Letters markets, we propose to establish a USP access condition that requires Royal Mail to offer access at the IMC for the provision of D+2 and later than D+2 Letters and Large Letters services.

### **Setting the terms and conditions of access**

- 9.15 The Act provides a framework for imposing certain types of obligation in USP access conditions as well as power to specify or describe terms and conditions that Royal Mail must include in the terms and conditions that it offers access users. Beyond that, it is left to Ofcom to determine the precise content of the obligations to be included in the condition as well as, more generally, the extent to which it is appropriate to become more involved in setting the detailed terms and conditions of access.
- 9.16 In the October consultation (Annex 7: paragraphs 3.17-3.28) we proposed that commercial negotiations between Royal Mail and access operators should provide the basis for agreeing the terms and conditions of access. Therefore, although we recognise that the Act permits Ofcom to include in a USP access condition a provision requiring that Royal Mail offers access on the terms and conditions as may be specified by Ofcom, we do not believe that such a prescriptive approach is appropriate.
- 9.17 Instead, we proposed that the USP access condition should include a more general requirement that the terms and conditions of access (including prices) offered by Royal Mail should be "fair and reasonable". This would provide Royal Mail with greater flexibility to negotiate the terms and conditions of access with access users.
- 9.18 In addition to imposing a general obligation for terms and conditions to be offered on a "fair and reasonable" basis, we also proposed that the guidance document referred to above would include an explanation as to how Ofcom would approach assessing whether the terms and conditions of access had been offered on a fair and reasonable basis.
- 9.19 In addition to the provision of guidance, our analysis indicates that there are a limited set of areas which are key to the effectiveness of the access regime, and where we

consider that further detail should be included in the USP access condition. More specifically, we propose that the USP access condition should include:

- A requirement for Royal Mail to provide a transparent and objective process for postal operators and users of postal services to request access contracts or variations to existing contracts;
- A requirement for the notification and publication of changes to prices, terms and conditions; and
- A requirement to offer information relating to the Quality of Service.

9.20 These are discussed further below.

#### Process for requesting access contracts and variations to existing contracts

9.21 We propose that the USP access condition should include a requirement for Royal Mail to adopt a reasonable, transparent and timely process for postal operators and users of postal services to make requests for access contracts (or variations to existing access contracts).

9.22 We consider that Royal Mail, through consultation with industry, should be well placed to develop the specific details of such a process. Therefore, we propose that Royal Mail publishes a statement setting out the process for requesting access contracts or variations to existing contracts (a “statement of process”), having previously consulted with the industry on its proposed process.

9.23 We propose that the USP access condition should state that, in developing its statement of process, Royal Mail must address the following key areas:

- How access requests should be made;
- The basic information that is required from an access seeker to progress an access request and an appropriate means of providing such information; and
- A set of timescales in which Royal Mail will handle requests for access (or variations to existing contracts).

9.24 We propose that Royal Mail should consult and publish its statement of process within three months of the USP access condition being imposed. We would then expect the processes set out in the statement to be followed by Royal Mail in handling any future requests for access and variations to existing access contracts, subject only to a right for Ofcom to direct Royal Mail to change the terms of the statement of process or the manner in which they are to be applied.

9.25 We recognise that under our proposals there would be a period of time between the USP access condition coming into effect and Royal Mail adopting the statement of process. In this interim period, we would expect that the current processes for agreeing access contracts and variations to existing contracts would continue to apply.

#### Notification and publication of terms and conditions

9.26 Currently, all access contracts are substantially the same as each other and there are only a limited number of provisions that have been individually negotiated. We

recognise that, in the future, the industry might wish to achieve greater flexibility to negotiate individual agreements. One way that that might be achieved would be if Royal Mail provided all customers with a standard set of terms and conditions of access, but was free to negotiate other aspects of the contracts with individual access customers. Therefore, given the possibility of alternative contractual frameworks, we have developed our proposals for the notification and publication of terms and conditions such that they would remain applicable regardless of which approach to the setting of standard terms and conditions applied.

- 9.27 We have included in the draft USP access condition a requirement for Royal Mail to publish standard terms and conditions and to ensure that an up-to-date set of terms and conditions remains publicly available. We have defined standard terms and conditions to mean such terms and conditions that are common to all D+2 Access Contracts or, where D+2 Access Contracts are individually negotiated, such standard terms and conditions that are appended to such D+2 Access Contracts. The purpose of this definition is to capture both the current situation where all access operators have substantially the same access contract and any future situation where there is a core set of standard terms and conditions that apply to all contracts with other terms and conditions being individually negotiated.
- 9.28 The specific details of our proposals for notification and publication of standard terms and conditions are set out below. Our intention is to require Royal Mail to give appropriate notice of changes to the standard terms and conditions and be under an obligation to publish such changes in a manner that meets the reasonable needs of access users. We believe that such a requirement is necessary so that access operators are able to manage appropriately any changes to the terms of access with their own customers and maintain a sufficient level of transparency to the access regime.
- 9.29 To be clear, these proposals relate to standard terms and conditions only and are not proposed to apply to individually negotiated terms and conditions (where the period for implementing the changes to the terms and conditions is expected to be agreed as part of the negotiation process).

### *Price*

- 9.30 So far as changes to access prices are concerned, we propose that the USP access condition should include a requirement for Royal Mail to provide access operators with ten weeks' notice of changes to price (unless otherwise agreed with the access operator) and that Royal Mail be required to publish such changes at the same time as providing notice.
- 9.31 We consider that our proposal provides an appropriate period for access operators to manage a price change with their end customers, recognising that a ten week period is consistent with the current contractual requirements which appear to have worked effectively. We believe that a shorter notification period could jeopardise the ability of access operators to properly manage the process with their end customers whilst a longer period appears to be unnecessary.

### *Non-price terms – notification*

- 9.32 In relation to our proposals regarding Royal Mail's notification requirements for non-price terms, we have reflected on the contractual notification requirements in the existing access agreements.

- 9.33 In this regard, we are aware that, for some terms, Royal Mail is unable to make changes unless agreed with the access operator (i.e. mutual agreement is necessary). Here we consider that notification is largely irrelevant given that Royal Mail has to gain agreement from the customer to make the change and that the length of period before the change is implemented can be determined as part of that agreement.
- 9.34 For other provisions included in the existing access agreements, largely around operational requirements, Royal Mail is able to make unilateral changes subject to providing advanced notice ranging from one to six months depending on the provision in question. Therefore, in cases where Royal Mail is able to make unilateral changes to non-price terms the notice period for the change is set out as part of the contract.
- 9.35 We recognise that there could be circumstances under the current contractual arrangements where it is unfeasible for Royal Mail to make changes to the standard terms and conditions of access because it cannot make the specific change unilaterally and it is unable to agree the changes with all of its access customers without engaging in an overly onerous process of individual negotiation and potentially recourse to the regulator. Such circumstances may be of detriment to the access regime as a whole.
- 9.36 Therefore, an alternative option that could be taken forward for consideration by the industry is for Royal Mail to have the ability to make unilateral changes to more, or all, standard terms and conditions. We consider that the feasibility and acceptability of such an option would be dependent on Royal Mail providing a sufficient period of notice in relation to changing the terms and conditions (or different categories of terms and conditions) as is appropriate for the purposes of a) enabling the access operators to manage the impact of those changes and b) to bring disputes in the event that they disagreed with the changes being proposed.
- 9.37 We have therefore developed our proposals for the notification of changes to non-price standard terms and conditions with both the current contractual arrangements in mind (i.e. recognising that changes to certain terms and conditions currently require the prior consent of the access operators whilst others can be changed unilaterally by Royal Mail) and also any future contractual arrangements where Royal Mail has greater flexibility to change standard terms and conditions unilaterally.
- 9.38 In recognition of the need for Royal Mail to provide sufficient notice of unilateral changes, we have proposed including a requirement for Royal Mail to publish a statement setting out the various periods of notice that it must give access operators for each of the different categories of terms and conditions where the contract allows it to make unilateral changes. Ofcom has reserved the right to intervene to direct Royal Mail to offer a different period of notice in the event that we consider that the period of notice set out in the statement is insufficient for changes to any particular categories of terms and conditions.

#### *Non-price terms – publication*

- 9.39 We are not proposing that any changes are required to the requirements and notice periods laid out in the contracts. However we consider that there is a benefit to having a transparent requirement around publication of changes to standard terms and conditions which will be consistent across any future changes to the contractual framework for access, and potentially across different types of changes to terms.

- 9.40 We consider that a publication requirement of ten weeks in advance of the implementation of changes to non-price terms that accords with our publication proposals for price terms is the clearest approach to providing transparency regarding the standard terms and conditions of access. As with changes to prices, this would be subject to agreement of a shorter publication period between the parties (similar to our proposals for the notification of changes) such as in relation to the current publication requirement of one month which applies in some cases within the current contract.
- 9.41 To be clear, the options presented above relate to Royal Mail's requirements to notify and publish changes regarding standard terms and conditions. For non-standard terms, Royal Mail's requirement to notify changes would be subject to the individual agreement and there would no requirement to publish.
- 9.42 In summary, we propose that the USP access condition require Royal Mail to provide sufficient notice of changes to such terms and conditions to access operators as follows:
- 10 weeks prior publication and notification of standard price terms (unless otherwise agreed);
  - 10 weeks prior publication of standard non-price terms (unless shorter notification period agreed, in which case consistent with shorter period);
  - A transparent process for prior notification of those non-price changes that do not require the prior consent of the access operator, with periods sufficient to allow operators to manage the impact of such changes; and
  - No requirements around notification or publication for individually negotiated terms.
- 9.43 For the avoidance of doubt, none of these changes is intended to override the requirements of the existing contracts for Royal Mail to provide advance notification and/or to agree changes to terms and conditions with its customers. Our proposals are intended to provide a robust and transparent approach to notification and publication which can be applied across current or future agreements between Royal Mail Wholesale and its access customers.

### Quality of Service

- 9.44 We consider that it is important that access users are able to monitor the QoS that Royal Mail provides in relation to delivering access items following injection into Royal Mail's network. Therefore, we propose that the USP access condition should include a requirement for Royal Mail to provide access users with QoS information based on a fair and reasonable system of monitoring QoS.
- 9.45 In proposing a Quality of Service requirement in the USP access condition, we note that Royal Mail has invested in a system that allows the monitoring of the QoS of access items. The information obtained from Royal Mail's system is used to determine whether Royal Mail has met its contractual QoS target and thereby determine whether access users are entitled to compensation for under performance. Royal Mail should therefore be able to continue to use and build on its existing system, without significant further investment, to obtain information that fulfils the proposed requirement in the USP access condition to provide QoS information.

- 9.46 We wish to make it clear that Ofcom is not proposing to set Quality of Service levels as part of the USP access condition. We consider that setting a Quality of Service standard level or levels would be inappropriate given that we are not proposing to set access prices either. However, we recognise that there is likely to be a trade-off between QoS levels and prices and therefore through the provision of QoS information, Ofcom and customers will be able to assess whether Royal Mail is providing access on fair and reasonable terms.
- 9.47 In our October consultation (paragraphs 4.18 and 4.28), we raised the issue of whether an end-to-end QoS metric would be of benefit to customers that have agreements with access operators. An end-to-end measurement of QoS could provide sending customers with information about the QoS from the collection of mail from the customer by the access operator to hand-over to Royal Mail at Mail Centre. This would supplement information that is currently measured regarding the QoS from the hand-over of items by access operators to Royal Mail at the Mail Centre to delivery.
- 9.48 As set out in our October consultation, we consider that end-to-end QoS information could be of benefit to customers. However, we consider that the demand for such information should be customer led and that, if there is a genuine demand from customers, industry should endeavour to reach an agreement regarding how the customer demand is most appropriately satisfied.
- 9.49 Consequently, we do not believe that it is appropriate for Ofcom to intervene in this matter at this time. However, notwithstanding this view, we are interested to hear from customers as to whether information relating to the end-to-end QoS is of benefit and whether they are confident that the market can adequately satisfy their demands. Ofcom intends to monitor developments in relation to this issue.

*Q9.1 Do you agree with our proposals for the process for applying for access agreements (and variations to existing agreements); notification and publication requirements; and quality of service requirements? If not, please provide your reasons.*

### **Principles for addressing issues of non-equivalence**

- 9.50 Areas where there are differences between the terms of access offered to third parties compared to those offered to Royal Mail's own business in relation to accessing Royal Mail's postal network are sometimes referred to as issues of 'non-equivalence'.
- 9.51 In our October consultation (Annex 7: paragraphs 4.19 – 4.29), we proposed that ensuring equivalence should align with the concept of no undue discrimination or no undue preference. Therefore, we proposed that the USP access condition should include a requirement that Royal Mail should not discriminate unduly against any particular persons or against a description of persons in relation to access matters.
- 9.52 We proposed (Annex 7: paragraph 4.22) to address issues of non-equivalence either through seeking to impose an operational change on Royal Mail or through taking account of any cost differential that results from the issue of non-equivalence in the transfer price as part of the margin squeeze control arrangements or in the transfer price under a future monitoring regime.



- 9.53 However, beyond the requirement not to discriminate, we do not propose that any of the areas of non-equivalence highlighted through the consultation process need to be specifically included in the USP access condition.
- 9.54 As discussed below, we consider that the dispute resolution process may provide an appropriate means for access operators to seek to resolve concerns over potential issues of non-equivalence.
- 9.55 In addition, there could be circumstances where Ofcom may consider taking enforcement action against Royal Mail for breach of the non-discrimination obligation in the USP access condition.
- 9.56 Ofcom has noted the undertakings that Royal Mail made to Postcomm relating to the 'ring-fencing' of Royal Mail Wholesale.<sup>102</sup> Ofcom considers that the need to ensure that Royal Mail maintains a ring-fence around Royal Mail Wholesale continues to be important under the new regulatory regime. Furthermore, in the absence of a requirement in the condition, we would not expect individual access operators to agree such 'ring-fencing' arrangements with Royal Mail.
- 9.57 Therefore, in order to ensure that Ofcom would have a basis for taking enforcement action in the event that Royal Mail did not comply with those undertakings, we propose a continuation of those elements of USPA 3 that prohibit Royal Mail from obtaining any unfair commercial advantage for itself or any other party in connection with the provision of access to its postal network. This includes the requirement for Royal Mail to use all reasonable endeavours not to disclose any information it receives from providing access to its postal network for the benefit of or use by any of its own trading businesses or any related person.
- 9.58 We therefore propose that the requirement for Royal Mail not to obtain any unfair commercial advantage be included with the non-discrimination requirement in the USP access condition.

### **Preventing price squeeze**

- 9.59 Under the Act, Ofcom has the power to impose a price control on access pricing where it appears to Ofcom that such a condition is necessary to prevent the universal service provider from setting excessive prices or engaging in a price squeeze between retail and access prices.
- 9.60 As we explained in our October consultation (Section 6), we do not consider that it is appropriate to impose on Royal Mail a price control to address the risk of excessive pricing. By contrast, we do have concerns about a risk of price squeeze and have therefore focussed on how we propose to address these concerns.
- 9.61 Our preferred long-term approach to addressing the risk of price squeeze is to monitor Royal Mail's costs and revenues to assess the impact of its pricing on competition (as opposed to imposing ex ante controls on Royal Mail's pricing). In addition, in relation to setting prices we consider that LRIC costs provide the correct signals for entry in the market and that Royal Mail should set its prices such that a

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<sup>102</sup> Postcomm, Condition 10 of Royal Mail's Licence: Prohibition against Obtaining Unfair Commercial Advantage, A Complaint about Royal Mail's Offer of Zonal Downstream Access, Second Report and Decision of the Postal Services Commission, July 2006.

minimum of LRIC margin is maintained between its access prices and the equivalent retail prices.

- 9.62 However, we recognise that robust LRIC information is not currently available and that before relying on a monitoring regime we would need to be satisfied that our other regulatory safeguards relating to cost transparency and accounting separation had been successfully implemented.
- 9.63 Given these considerations, we proposed (Annex 7: paragraph 7.38 in that earlier consultation) to impose a margin squeeze control in relation to access pricing that is broadly consistent with the principle of monitoring but with additional safeguards requiring Royal Mail to provide evidence to us that it expects to meet specified tests in the control.
- 9.64 We proposed (Annex 7: paragraph 7.42) that the scope of the margin squeeze control should include Mailsort 2 and Walksort 2 Letter and Large Letter products only. We proposed (Annex 7: paragraphs 7.46 – 7.50) that the margin squeeze control be comprised of two elements: (a) a margin squeeze 'basket'; and (b) a 'price point' control.
- 9.65 In relation to the margin squeeze basket, we proposed (Annex 7: paragraph 7.55) that Royal Mail should be required to demonstrate having a reasonable expectation of recovering a minimum level of upstream relevant costs across the basket of products within the scope of the control. We proposed that Royal Mail's relevant upstream costs be based on Royal Mail's upstream FAC costs with adjustments. More specifically we proposed (Annex 7: paragraph 7.47):
- Upstream FAC is calculated as Royal Mail's end-to-end FAC less the equivalent access FAC (including Royal Mail Wholesale costs). In calculating relevant upstream FAC we proposed:
    - Excluding a set of specified costs that is non-incremental to upstream activities – an allocation of central overhead costs from Royal Mail's upstream FAC (estimated to be between 5%-10% of FAC); and
    - Including an adjustment to FAC for a reasonable rate of return (estimated to be between 5%-10% of revenue).
- 9.66 Given that the above adjustments are expected to broadly net to zero, we propose that they are assumed to be equal within the access condition, and no specific adjustment is made for either. We also propose that no adjustment is required for 'exceptional' costs, through using a FAC measure which does not include such costs.
- 9.67 As discussed further above, we may consider adjustments to the cost measure to reflect equivalence differences between Royal Mail's retail and wholesale services. We propose that the definition of costs to be used in the margin squeeze test include a figure to represent such equivalence differences. Should Royal Mail or an access operator approach Ofcom with an area of non-equivalence which we considered required an adjustment, we propose being able to direct that this would be included in the calculation. For the avoidance of doubt, unless and until we are provided with such evidence, the level of equivalence differences will be taken to be zero.
- 9.68 In relation to the 'price point' control, we proposed that Royal Mail be required to demonstrate having a reasonable expectation of recovering a minimum of 50% of relevant upstream FAC for individual contracts. We propose that this would apply to

each individual price point that is offered by Royal Mail for the services included in the scope of the margin squeeze control (i.e. in relation to the individual product, format and weight step).

- 9.69 In demonstrating that it had a reasonable expectation of meeting the requirements of the control, Royal Mail would be required to provide a forecast of the forthcoming period's costs, volumes and revenues. We proposed that the information be provided to Ofcom on a quarterly basis. We are proposing within the condition that the test be on an annual basis, to avoid the impact of seasonality of revenues or cost fluctuations, but we expect that there should be quarterly compliance reporting. We are not proposing specific requirements for the contents of the report, other than that it should provide sufficient information.
- 9.70 Under our proposals we recognise that unforeseeable changes in volumes and costs could result in Royal Mail not recovering its relevant upstream costs in the relevant period. Under such circumstances and, in assessing whether Royal Mail had met the requirements of the control, Ofcom would be likely to consider the assumptions that Royal Mail had made in setting prices, estimating costs and estimating volumes with regard to meeting the requirement of the control. If the changes in volume and costs were genuinely unforeseeable, we would not be likely to consider Royal Mail to have breached the requirements of the control, although we would of course have to consider each case on its own merits.
- 9.71 We propose that the requirements of the margin squeeze control (including a requirement for Royal Mail to provide Ofcom with information that demonstrates it has a reasonable expectation of meeting the control) will be included in the USP access condition.

### **Process for addressing disputes**

- 9.72 In our October consultation, we proposed (Annex 7: paragraph 5.11) to adopt the dispute resolution process for access that has been previously established by Ofcom for the communications sector in its Dispute Resolution Guidelines<sup>103</sup>, subject to recognising any appropriate differences such as where the Communications Act and the Act impose different legal requirements.
- 9.73 We have already published an explanation of the format for submitting a dispute referral to Ofcom<sup>104</sup> which should be read in conjunction with Ofcom's Dispute Resolution Guidelines by any postal operator or user of postal services considering referring a dispute to Ofcom once the USP access condition is in place.
- 9.74 As noted above, there are differences between the Communications Act and the Act which affect the Dispute Resolution Guidelines. For example, references to sections 185-191 of the Communications Act which govern disputes brought under the Communications Act should be read as references to Part 2 of Schedule 3 of the Act which govern access disputes in post.
- 9.75 In light of those differences, we are considering the need to publish a further document which identifies more specifically the parts of Ofcom's existing Dispute

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<sup>103</sup> Ofcom *Dispute Resolution Guidelines – Ofcom's guidelines for the handling of regulatory disputes*, 7 June 2011 [http://stakeholders.ofcom.org.uk/binaries/consultations/dispute-resolution-guidelines/statement/Dispute\\_Resolution\\_Statement.pdf](http://stakeholders.ofcom.org.uk/binaries/consultations/dispute-resolution-guidelines/statement/Dispute_Resolution_Statement.pdf)

<sup>104</sup> See Annex 6 of the Statement "Postal regulation: Transition to the new regulatory framework" dated 29 September 2011.

Resolution Guidelines which would be different for postal access disputes. However, at this stage it is worth noting the two key differences between the Communications Act and the Act that are pertinent to Ofcom's processes for handling such disputes. These are as follows:

- The Communications Act lays down a four-month timetable for resolving disputes (except in exceptional circumstances). The Act does not impose any such deadline for resolving disputes in relation to access matters in post. Instead, Ofcom must resolve the dispute "as soon as reasonably practicable". Notwithstanding the difference between the Communications Act and the Act, Ofcom recognises the importance of resolving disputes in relation to access matters in post in a timely manner. We will endeavour to resolve postal disputes within four months as well.
- Under the Communications Act, there are certain circumstances in which Ofcom has relatively little discretion about whether it is appropriate for it to handle a dispute. However, under the Act, Ofcom has broad discretion in deciding whether it is appropriate to accept a dispute in relation to postal access matters.

9.76 Under our proposals, an access user would be able to refer an access dispute to Ofcom in accordance with the provisions set out in Schedule 3 of the Act. Since these provisions apply in any event, we do not consider that it is necessary to make further provision in the USP access condition in this regard.

## **How we envisage our proposed regulatory framework for access will work in practice**

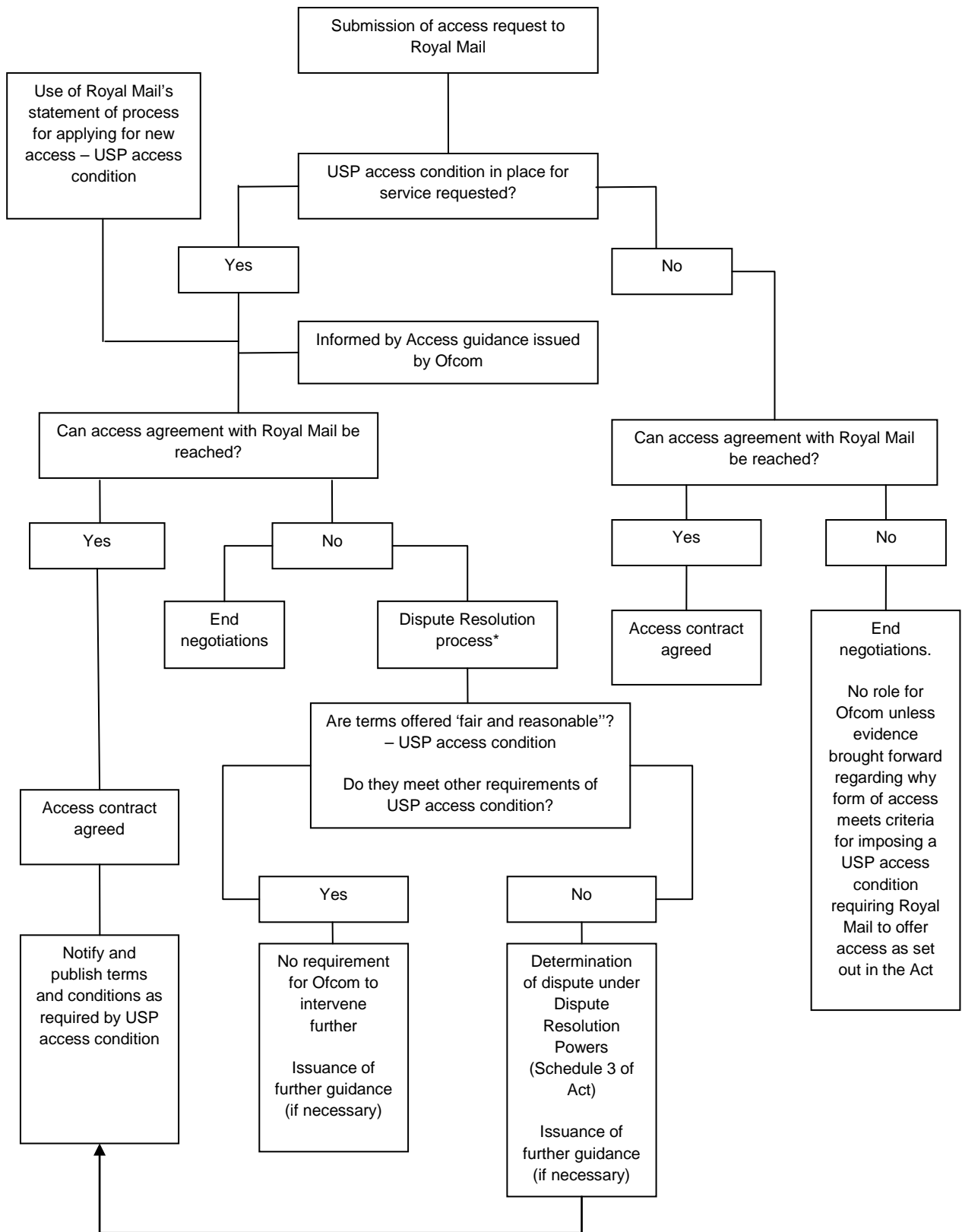
9.77 In our October consultation (Section 7 and Annex 7) we outlined our proposals for regulating access from 2012. In this document, we have provided supplementary proposals around some of the more detailed aspects of the implementation of our proposed regulatory framework for access as well as details of how this will be enacted through a USP access condition.

9.78 In this subsection of the document, we provide a guide to how we believe that our proposals will operate in practice. We recognise that we are currently consulting on our proposals and that responses to these could have a bearing on some of the more detailed elements of how the access regime will operate. Nevertheless, we consider that providing a guide at this stage, and in advance of March 2012, will be of value to stakeholders. Stakeholders should note that the charts set out below are illustrative, and that in individual cases certain elements may be subject to change, including in particular the questions that Ofcom considers need to be answered in order to resolve any particular dispute.

9.79 We set out the process that would apply for these circumstances:

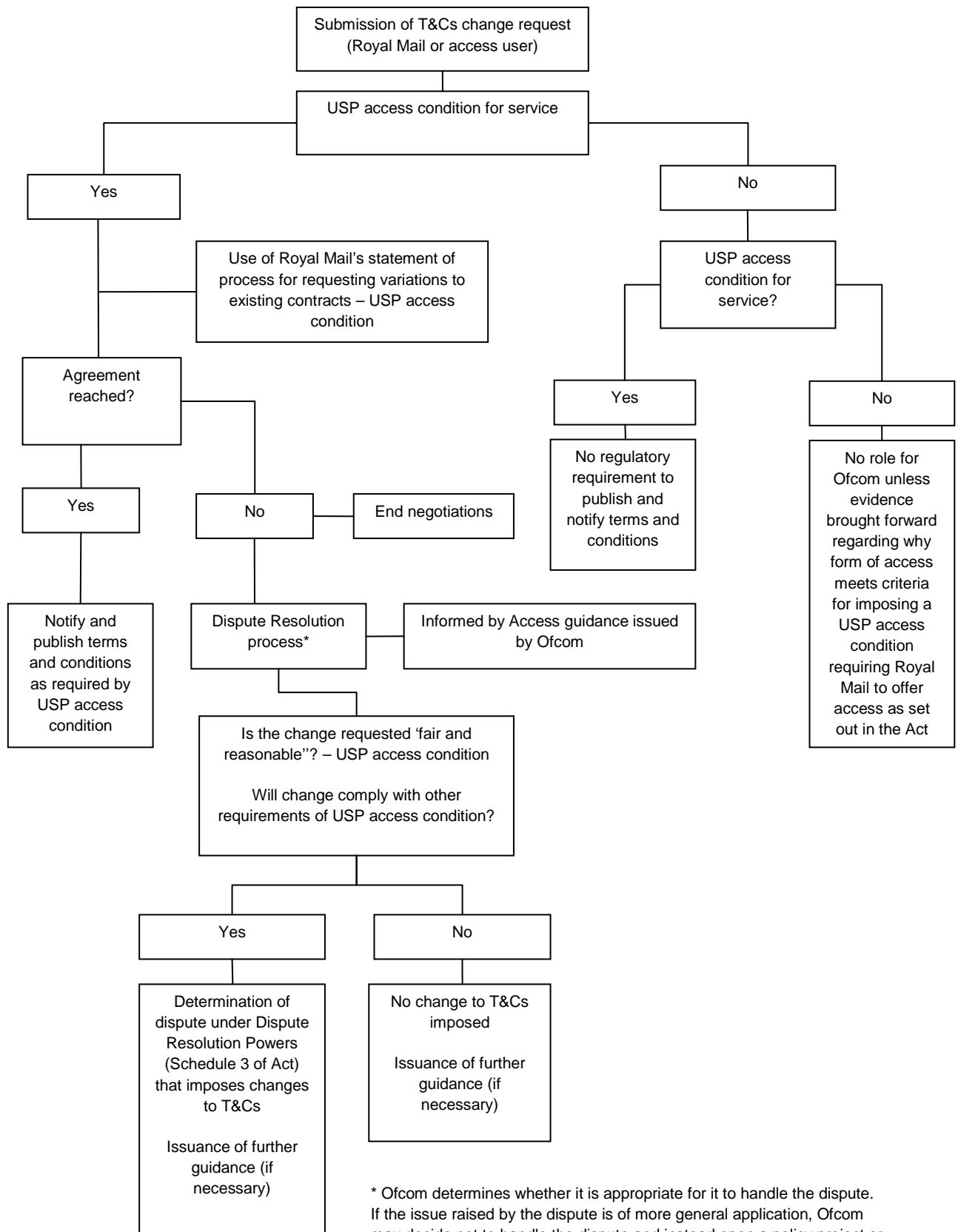
- Requesting a new access agreement;
- Requesting a change to the terms and conditions of an existing access agreement; and
- Raising an issue regarding the interpretation of a condition of access or raising an equivalence challenge.

**Figure 1: Process for requesting a new access agreement**



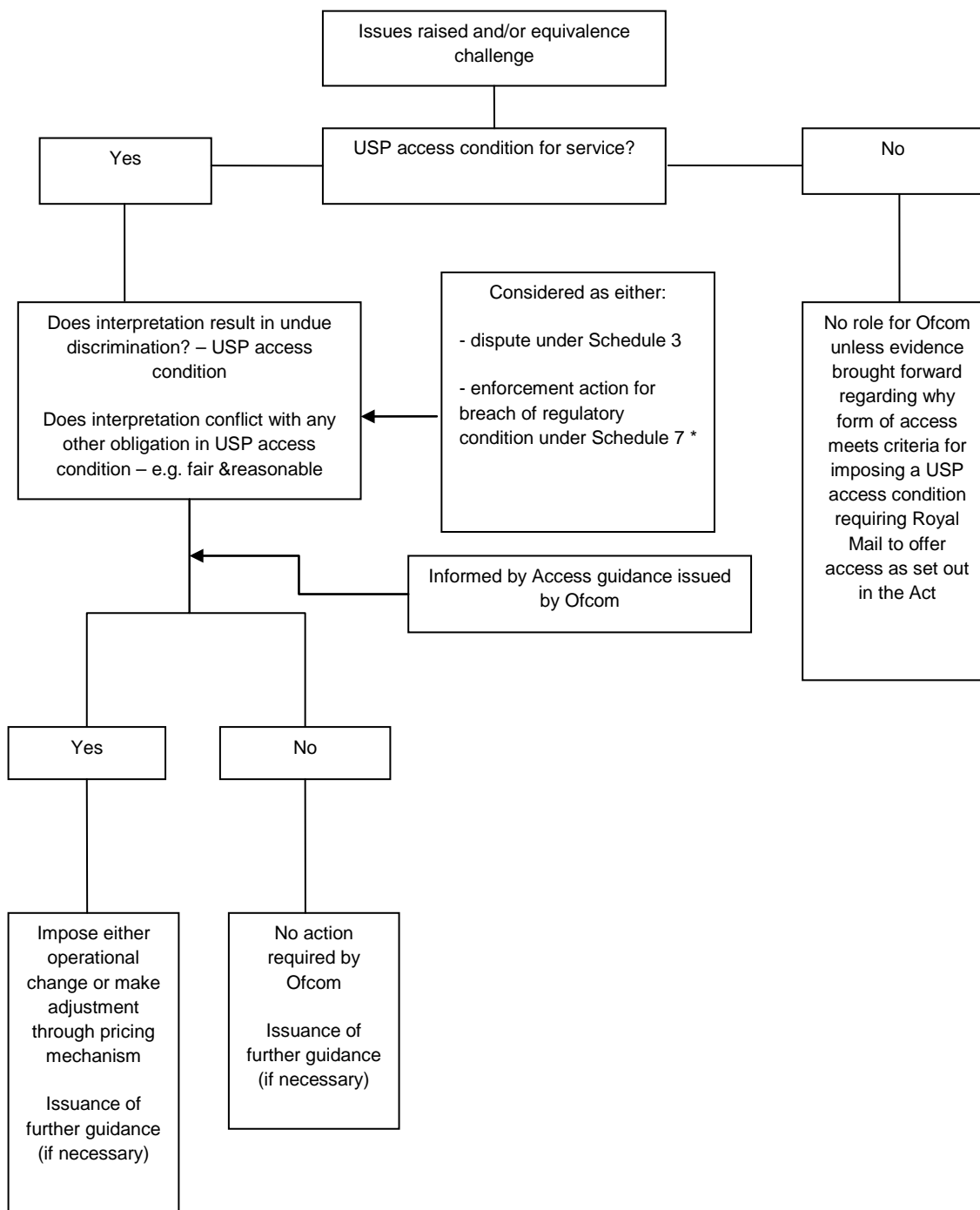
\* Ofcom determines whether it is appropriate for it to handle the dispute. If the issue raised by the dispute is of more general application, Ofcom may decide not to handle the dispute and instead open a policy project or take enforcement action.

Figure 2: Requesting change to existing terms and conditions of access



\* Ofcom determines whether it is appropriate for it to handle the dispute. If the issue raised by the dispute is of more general application, Ofcom may decide not to handle the dispute and instead open a policy project or take enforcement action.

**Figure 3: Raising an issue regarding the interpretation of a condition of access or an equivalence challenge**



\*In any event, Ofcom may be able to use ex post competition powers to address such issues.

## Summary of our proposals

9.80 We propose that the USP access condition – set out in Annex 12 - will include:

- An obligation on Royal Mail to offer access to its network at the IMC for the purpose of providing D+2 and later than D+2 Letters and Large Letters services;

In addition and in reference to the above form of access:

- A requirement to provide access on reasonable request and to offer such access on 'fair and reasonable' terms;
- A requirement for Royal Mail to publish a statement of process for agreeing access contracts and variations to existing contracts;
- A requirement to notify and publish standard terms and conditions (including charges);
- A requirement to monitor the Quality of Service of access services;
- A requirement not to unduly discriminate;
- A requirement that prohibits the gaining of an unfair commercial advantage from allowing access to the network and seeks to ensure that Royal Mail does not use information in its possession as a result of giving access for its benefit; and
- A requirement to set access prices to maintain a minimum level of margin between access prices and analogous retail services and for Royal Mail to provide Ofcom with information that demonstrates compliance with the requirements of the margin squeeze control.

## Legal tests

9.81 In Section 9 of the October consultation, we provided an assessment of how our proposals for the USP access condition meet the specific legal tests set out in the Act that need to be satisfied in order to impose such a condition. We consider that the assessment set out in that document applies equally to the supplementary proposals set out in this document. The supplementary proposals essentially address the details of how the USP access condition is to be implemented and can therefore be justified on the same basis as the main proposals set out in the October consultation.

*Q9.2 Do you agree with the proposals for establishing a USP access condition set out above? If not, please provide your reasons.*



## Section 10

# Implementing our proposals on regulatory accounting

## Appropriate financial and accounting records and reporting

- 10.1 The initial condition ACC 1 (previously licence condition 15) requires Royal Mail to maintain appropriate accounting and financial records.
- 10.2 A fundamental requirement of the existing condition is that Royal Mail's costing methodology must comply with the Costing Methodology Guiding Principles and Methodological Principles defined in the condition. Royal Mail must also maintain a Costing Manual which gives a full description of its costing methodology and the data sources used within it.
- 10.3 The condition also sets out the process for initiating and notifying changes to the Methodological Principles and the Costing Manual - as well as the respective roles of Royal Mail and Ofcom in this process. For instance, it explains in which cases Ofcom's consent would be required to changes initiated by Royal Mail.
- 10.4 Further, the condition requires Royal Mail to produce an income statement, balance sheet, and cash flow statement for each of the Existing Services as defined in the condition. It also refers to the requirements set out in the Accounting Separation Commitments document<sup>105</sup> which Royal Mail needs to fulfil.
- 10.5 Finally, the condition sets out the process for when and how Royal Mail should submit its regulatory financial statements to Ofcom as well as the related auditing and publication requirements.

## Proposals in the October consultation

- 10.6 In accordance with the Act, we must have regard to the need for the provision of a universal post service to be financially sustainable, and for it to be efficient before the end of a reasonable period and for its provision then to continue to be efficient at all subsequent times.
- 10.7 In light of the above in the context of the current state of Royal Mail's business and the postal services market, we proposed, in our October consultation, to give Royal Mail greater commercial freedom subject to appropriate regulatory safeguards. That document contains the impact assessment of our proposals.
- 10.8 These safeguards should include effective monitoring of Royal Mail's conduct and performance. We considered that there were minimum safeguards that need to be in place for any monitoring regime, including cost transparency and accounting separation measures.

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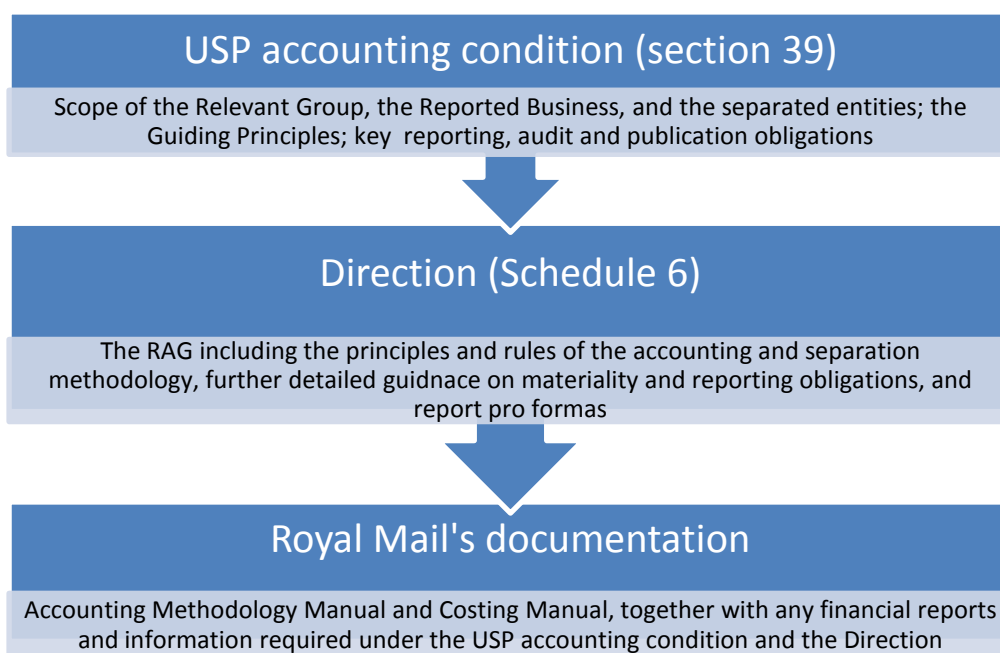
<sup>105</sup> Published by Postcomm in February 2011 entitled "Laying the foundations for a sustainable postal service", Explanatory memorandum and notice of proposed licence modifications under section 14 of the Postal Services Act 2000"

- 10.9 As set out in our October consultation, we therefore proposed a new regulatory financial reporting framework for Royal Mail implemented by a revised USP Accounting condition, which incorporates new cost transparency and accounting separation measures. We discussed in the October consultation the need for the regulatory financial reporting obligations that we are proposing to impose on Royal Mail, including their aims, and the reasons why we consider it would be proportionate to impose them. The objectives of the new regulatory financial reporting include the following:
- Monitoring the financial sustainability of universal service provision;
  - Monitoring the efficiency of universal service provision;
  - Understanding how costs and revenues are apportioned to different products and activities; and
  - Monitoring the relative profitability of different product groups sharing activities and costs.
- 10.10 Compared with the requirements of the initial condition, the new regulatory financial reporting requirements proposed for the revised USP Accounting condition aim at providing a higher level of transparency which is necessary for our proposed monitoring regime.
- 10.11 The main financial regulatory reporting proposals in the October consultation were, in summary, to require Royal Mail to:
- Report separately on different parts of its business relevant to our regulatory duties;
  - Improve further the documentation of costing and regulatory accounting more generally;
  - Increase the extent of relevant financial information that is published on a regular basis; and
  - Enhance the level of assurance that we can place on the financial information reported for regulatory purposes.
- 10.12 In this respect our key regulatory financial reporting proposals, set out in detail in Section 8 and Annex 6 of our October consultation, were as follows:
- **The Relevant Group** is defined as Royal Mail Group Limited ('RMG') and all of its subsidiary and associated undertakings, excluding Post Office Limited ('POL');
  - **The Reports for the Relevant Group** should comprise financial statements, annual updates to the Strategic Plan, and quarterly cash flow projections, which should be provided to assist in the monitoring of the overall financeability of the universal service provider;
  - **The definition of Reported Business** for the remaining regulatory financial reporting obligations should correspond to the scope of activities in Royal Mail's integrated costing methodology with the associated reporting used to assess the financial sustainability and efficiency of the activities used for the provision of the universal service;

- **The regulatory reporting for the Reported Business** should include quarterly unaudited, and annual audited, income statement information to the level of Earnings before Interest and Tax ('EBIT'), and consistent operational balance sheet and cash flow information;
- **The separate financial reporting of elements of the Reported Business**, provided both quarterly (unaudited) and annually (audited) should include published income statement information to the level of EBIT, split between four separated financial reporting entities ('FREs') as well as between universal service and non-universal service products and for non-Mails products, as well as (mainly confidential) product profitability information;
- **Royal Mail's national costing methodology** should be updated in 2012-13, in particular to reflect our proposals for further improvements in transparency and cost orientation;
- **Royal Mail's zonal costing methodology** should be subject to improved regulatory oversight in 2012-13;
- **The requirements for regulatory financial reporting should be more specific** and set out in Regulatory Accounting Guidelines ('RAG') published by Ofcom, covering the principles and rules based on which Royal Mail should prepare regulatory financial reports from 2012-13;
- **Royal Mail should prepare documentation and manuals**, setting out how it is meeting these requirements, and containing appropriate levels of detail, include these within a new Accounting Methodology Manual and an updated Costing Manual, with material changes notified to Ofcom; and
- **Assurance arrangements** should be revised, in particular a move to a tri-partite reporting arrangement for 2012-13 and a subsequent move to a 'fairly represents' form of audit opinion.

## Implementing our proposed approach to accounting and reporting via a condition

- 10.13 In our October consultation, we proposed to implement the above requirements by amending the existing USP Accounting condition (ACC 1) under section 39 of the Act and a supporting direction to specify the RAG. Under the Act any subsequent changes to the condition or the direction would be implemented following consultation.
- 10.14 In this consultation, we set out how the above proposed requirements would be reflected out in the proposed USP Accounting condition and supporting direction.
- 10.15 We propose that the fundamental reporting requirements, which derive their force directly from the Act, are set out in the proposed new condition itself; while the more detailed requirements are set out in the RAG by direction. On this basis the following diagram describes the proposed scope of the condition, the direction, and the documentation which Royal Mail will be required to prepare by the condition and the direction:

**Figure 4: Structure and hierarchy of regulatory obligations**

10.16 Drafts of both the USP Accounting condition, and the supporting direction containing the RAG, which we propose to put in place from the start of Royal Mail's 2012-13 financial year (26 March 2012) are set out in Annex 13 and 14. In these documents, we have made the following clarifications and additions in respect of our proposals set out in the October consultation:

- a) In the October consultation, we stated that we would consider the requirement for Royal Mail to continue to provide confidential monthly information. The draft USP Accounting condition and the supporting direction containing the RAG include this requirement.
- b) In the October consultation, we proposed that Royal Mail should provide us with supplementary outputs from its costing system to allow us to represent those outputs in our model (the Cost Allocation Model). The USP Accounting condition and the supporting direction containing the RAG have been drafted on the assumption that Technical Appendices to the Costing Manual will include all the information required to meet this requirement.
- c) In the October consultation, we proposed that Royal Mail should notify Ofcom, in advance, of any material changes made to its Costing Manual and Accounting Methodology Manual. In the USP Accounting condition, we have added the requirement, comparable to that in the existing USP Accounting condition, that Royal Mail should secure a statement by the Qualified Independent Auditor setting out whether or not Royal Mail has complied with the pre-notification requirement. In our view, this will allow Ofcom to continue to assess, in a timely fashion whether Royal Mail's regulatory accounting methodology continues to be in compliance with the USP Accounting condition and the RAG.
- d) We have added a clarifying standard requirement for Royal Mail to retain its financial and accounting records for six years.
- e) We have generalised the requirement in the Guiding Principles for the Regulatory Accounting Methodology to comply with the accounting standards in Royal Mail's

statutory accounts, subject to any departures directed by Ofcom from time to time;

- f) We have specified the lengths of the periods set out in the October consultation, and referred to in the condition (e.g. publication deadlines) from months into the equivalent number of days for the purposes of the legal documentation.
- g) We have also clarified in the USP Accounting condition what we mean by publication and delivery of the required financial information. In this context we have specified a first date for delivery of 25 March 2012 for the updated form of the Costing Manual, and a first date for delivery of 23 June 2012 for the new Accounting Methodology Manual. This is to give effective start dates for the reporting requirements including the change control processes set out in the Condition. We would welcome views as to the practicability of these timings.
- h) We have proposed a delivery date of 25 March 2012 for the first consolidated cash flow projection statement, and a delivery date of 23 June 2012 for the first annual update of Royal Mail's Strategic Business Plan, to allow Ofcom to commence the monitoring of the information provided in these documents for the first Financial Year of the USP Accounting Condition. We would welcome views as to the practicability of these timings.

- 10.17 It should be noted that in the draft of the USP Accounting condition, we have made reference to certain versions of documents (e.g. the initial scope of the Reported Business has been defined by reference to the most recent version of the Costing Manual expected to be available before the coming into force of the proposed new condition) and certain dates e.g. the dates set out in sub-paragraphs (g) and (h) above. These document versions and dates may need to be updated, or be otherwise changed, following the consultation.
- 10.18 In the October consultation, we explained how the relevant legal tests (objectivity, non-discrimination, proportionality, and transparency) were satisfied in relation to our proposals for regulatory financial reporting (without seeking to draw a detailed distinction between which of the financial reporting obligations proposed in that consultation would form part of the USP Accounting condition itself and which of them will be included in the direction).
- 10.19 In this consultation, we set out our proposed draft of the condition and direction which encompasses the RAG to provide stakeholders with further transparency in respect of the objectives and the legal implementation of our proposals.
- 10.20 Under the Act we may only impose or modify a regulatory condition such as the proposed USP Accounting condition if we are satisfied that the tests in Schedule 6 to the Act are met. A similar test also applies in giving, modifying or revoking directions<sup>106</sup>. In Section 9 of the October consultation we set out our assessment of how our proposals meet the legal tests set out in Schedule 6 of the Act, which we must satisfy in order to impose conditions such as these.
- 10.21 For ease of reference, we summarise below our main reasons why we consider that our proposals meet the relevant legal tests and duties specified in the Act in relation to our regulatory financial reporting proposals as a whole, without distinguishing

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<sup>106</sup> Paragraph 4(2) of Schedule 6 to the Act.

between the proposed financial reporting obligations imposed in the condition itself and the direction proposed to be issued under the condition. This assessment should, however, also be read in light of our overall proposals and considerations set out in the October consultation.

## Summary of our proposals

- 10.22 As explained above, in this consultation, we propose how the new regulatory financial reporting requirements set out in our October consultation - subject to us deciding to adopt those requirements after due consultation - should be set out in the new condition and direction.
- 10.23 We set out a draft of the new USP Accounting condition and the direction (including the RAG) in Annex 13 and 14, as well as an overview of the requirements set out in these documents within Annex 8.

## Legal tests

- 10.24 We are satisfied that our proposed regulatory financial reporting obligations satisfy the legal tests. We discussed our legal tests for creating this condition in paragraphs 9.54 to 9.63 of our October consultation. As we are simply setting out how we would implement those earlier proposals, we do not repeat that analysis here.
- 10.25 We were not able in the October consultation to address fully the requirement that any condition or direction should be transparent, as we did not at the time publish the text of the proposed USP Accounting condition and direction. This transparency consideration is now fully taken into account by our publishing, for consultation in this document, the proposed wording of the USP Accounting condition and the proposed wording of the RAG by means of a direction.
- 10.26 We further consider that the transparency of these proposed obligations is aided by our explanations in the October consultation in respect of the detailed proposals for the content of the USP Accounting condition and RAG in Annex 6 of that consultation.

*Q10.1 Do you agree that the new condition and the direction are appropriately set out to capture accurately, completely, and transparently, the regulatory financial reporting requirements we proposed in October consultation (as summarised above)? If not, please provide your reasons.*

## Section 11

# Our proposals regarding the transitory conditions

## The time limited conditions

- 11.1 A transitory condition is one which includes obligations which we would not have the power to impose under Part 3 of the Act. Some of the previous licence conditions were transposed as transitory conditions because they contained a mixture of obligations (i) some of which we would not have the power to impose under Part 3 of the Act, but also (ii) some of which we would have the power to impose.
- 11.2 All five of the transitory conditions mentioned are time-limited and will (assuming we implement our proposal to make an order under s.30 of the Act) cease to apply from the end of March 2012.
- 11.3 We have considered whether we should retain any aspects of these transitory conditions beyond that date. We note that if we were to retain any of their requirements we would effectively have to create a new regulatory requirement in a new (or within an existing) condition.
- 11.4 Below, we briefly discuss each transitory condition in turn – setting out what these conditions cover at the moment and what we are proposing to do going forward.

## Monitoring Compliance with quality standards

- 11.5 Transitory condition T 1 (previously in condition 4 of Royal Mail's licence) requires Royal Mail as the USP to appoint an official to monitor compliance with its quality standards and who is required to report to its board.
- 11.6 We are not proposing to retain any aspects of this condition going forward because we think it is inappropriate to prescribe the detail of how Royal Mail arranges its compliance with quality standards and to prescribe how this should relate to its own governance structure.
- 11.7 We note that we are proposing to retain the quality targets for universal services as set out in Section 5 and it will be necessary for Royal Mail to ensure it is able to organise its activities so that it can comply with that requirement.
- 11.8 We do not expect any negative impacts from our proposal on T 1. It may however remove a regulatory burden from Royal Mail.

## Compliance Officer Role and Compliance Reporting

- 11.9 This transitory condition T 2 (previously in condition 13 of Royal Mail's licence) requires Royal Mail to employ a 'Compliance Officer', to consult Ofcom on their appointment and to assign a number of compliance related tasks to this officer.
- 11.10 Royal Mail is also required to provide Ofcom with a full report after the end of the financial year which covers the compliance officer's activities with regard to USPA 1-3, CP 5, T 2 and s.18 of the Competition Act 1998 and the key activities of Royal

Mail's compliance function in relation to conditions DUSP 1-6, CP 1-2, E 1 and any information request issued by Ofcom under s55 of the Act during that year.

- 11.11 However, we note that we are proposing to retain the majority of reporting requirements in individual conditions which will help us to monitor Royal Mail's operational performance. If there are failures we may take enforcement action as appropriate. These reporting requirements require Royal Mail to provide data via quarterly and/or annual reports.
- 11.12 While we propose – in Section 5 - to remove reporting for non-universal services e.g. bulk mail and business collections, we propose to retain requirements for quarterly and annual reporting on universal service quality standards, quarterly reporting for Royal Mail's consumer complaints, an annual report on its compensation scheme for standards of service<sup>107</sup> and, as with other RPOs, Royal Mail will continue to have an obligation to provide an annual report on mail integrity and a separate annual report on misdirected / mis-collected mail.
- 11.13 In addition, we plan to use our information gathering powers for any additional data that we need, in future, to monitor Royal Mail's performance.
- 11.14 We do recognise that the compliance report has a slightly wider scope relative to the data reporting requirements that sit within individual conditions as it captures the current DUSP 1-3, CP 2 and access requirements. However, these conditions are areas where we intend to consider compliance on an on-going, rather than year-end basis, therefore making the annual compliance report of less use to us going forward.
- 11.15 As a result, we consider that retaining the compliance report requirement is unnecessary because there is no evidence that it would provide any additional value on top of the other means we can use to monitor Royal Mail's operational performance. Given this, we do not expect any negative impacts from our proposal to let T 2 cease. It would however remove a regulatory burden from Royal Mail.

### **Assurance of adequate necessary resources**

- 11.16 Transitory condition T 3 (previously condition 16 of Royal Mail's licence) also applies to Royal Mail and in short, requires it to provide Ofcom with an assurance from its directors that Royal Mail has access to the necessary resources – management and financial resources, physical assets, human resources and working capital – to provide specified postal services, or to alert Ofcom if it does not. The condition also requires Royal Mail to provide certain assurances if it wishes to pay dividends.
- 11.17 Section 8 of our October consultation proposed requirements on Royal Mail to provide reports and forecasts for the Relevant Group, and that should allow us to monitor its financial position going forward. In the context of these proposed reporting requirements, we do not currently consider that there is a need to place additional requirements on Royal Mail comparable to those in T 3.

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<sup>107</sup>We also note that Royal Mail has some requirements – within individual conditions – to publish information on their (independently audited) performance e.g. on quality of service. While Royal Mail will continue to have meet requirements with regard to the type of data to be published, they can decide themselves on whether it is better to publish this information individually or through a consolidated report.



- 11.18 Section 8 of our October consultation also highlights that changes to the structure of the Relevant Group may lead us to reassess some of the scope of the reporting requirements. In that context, and should there be a significant change to the way in which Royal Mail is financed, we could also revisit the need for some or all of the requirements sitting within the current T 3, with respect to the resources required to provide the universal service as part of the Relevant Group.
- 11.19 We do not expect any impacts from our proposal to let T 3 lapse. Again though, it would remove a regulatory burden from Royal Mail.

**Price controlled services, geographic price uniformity, non-priced services and non-price terms of regulated services**

- 11.20 Transitory condition T 4 (previously licence condition 21 of Royal Mail's licence) applies to Royal Mail as the USP and covers several different elements including requirements:
- a) to provide the regulated services on as wide a basis (geographically) within the UK as they were provided at end 31 March 2006;
  - b) to provide regulated services (other than access services) on terms other than price which are no less beneficial than those terms provided at end 31 March 2006;
  - c) to set prices for Controlled Services in such a way that they meets certain conditions; and
  - d) to provide some services free of charge – Return to Sender (as part of a regulated service); Certificate of Posting, Poste Restante, Petitions to Parliament and Petitions to Her Majesty the Queen.
- 11.21 In terms of the first requirement - (a) - we note that the Act requires Ofcom to secure universal access – which will mean customers must be able to send items to every home and premises in the UK or access the service from access points (post boxes and post offices for packets and registered items, post boxes for letters).
- 11.22 As set out in Section 5 we propose to secure this (as it is in fact currently secured) through the imposition of a DUSP condition. We believe that the cessation of this condition will have no impact on the geographical provision of the universal service and in particular no impact on the requirement for there to be UK-wide collections and deliveries. We consider it inherently unlikely that Royal Mail would cease to collect from or deliver to certain areas in respect of most non-universal services when it is required to go to them in the provision of universal services, but even in the event that this was wrong we consider that the universal service by definition incorporates the services that are required to be provided throughout the UK.
- 11.23 In terms of (b), we discussed our proposed approach to this requirement in Section 5, which relates to Royal Mail seeking approval (from Ofcom) before it seeks to make changes to the non-price terms of its universal service products. As set out in that Section, because we are now proposing to describe the characteristics of universal services, we propose to change to a different process whereby Royal Mail must now notify such changes (instead of seeking prior approval) although we would reserve the right to intervene if we do not believe the changes made were fair and reasonable.

- 11.24 Furthermore, (c) will no longer apply if we lift the price controls as we proposed in October consultation and therefore the numerous price control clauses in T 4 would fall away. That earlier consultation discussed the impacts of our proposal to grant Royal Mail commercial freedom for a period of seven years by not imposing a traditional price control subject to a number of safeguards.
- 11.25 Finally, with regard to (d) the obligation in respect of *Certificate of Posting, Poste Restante* and *Petitions* duplicates requirements of DUSP 1 so its lapse will not represent any change. In Section 4 we discussed our approach to the other service - *Return to Sender* – currently required by T4 to be provided free of charge and proposed there should be no ongoing requirement to provide it at no charge beyond 31 March 2012.

### **Common operational procedures – use of information**

- 11.26 Transitory condition T 5 (previously licence condition 14 of Royal Mail's licence and condition 4 of the Standard licence) applies to all RPOs and not just to Royal Mail. It requires them to refrain from using any information about the business of another postal operator, which it obtains from being party to a common operational procedures agreement, in order to secure unfair commercial advantage.
- 11.27 This condition does not fall within any of the condition types that may be imposed under Part 3 of the Act. However, we believe the risk may be managed by contract (including by postal operators proposing changes to the Postal Common Operational Procedures Agreement if relevant). Misuse of information may be subject to wider prohibitions, for example in some circumstances it may be prohibited by competition law. As we consider we cannot impose this requirement, it is not for us to assess the impact of its falling away.

### **Summary of proposals discussed in this Section**

- 11.28 We do not propose to create any regulatory requirements corresponding with those contained in any of the transitory conditions. If we make the order, these requirements will automatically cease to exist.

*Q11.1 Do you agree with our approach to the cessation of the transitory conditions – and if not, for which specific transitory conditions do you disagree and why?*

## Annex 1

# Responding to this consultation

## How to respond

- A1.1 Ofcom invites written views and comments on the issues raised in this document, to be made **by 5pm on 31 January 2012**.
- A1.2 Ofcom strongly prefers to receive responses using the online web form at <http://stakeholders.ofcom.org.uk/consultations/review-of-regulatory-conditions/> as this helps us to process the responses quickly and efficiently. We would also be grateful if you could assist us by completing a response cover sheet (see Annex 3), to indicate whether or not there are confidentiality issues. This response coversheet is incorporated into the online web form questionnaire.
- A1.3 For larger consultation responses - particularly those with supporting charts, tables or other data - please email [RRC@ofcom.org.uk](mailto:RRC@ofcom.org.uk) attaching your response in Microsoft Word format, together with a consultation response coversheet.
- A1.4 Responses may alternatively be posted or faxed to the address below, marked with the title of the consultation.

### **Chris Rowsell**

Floor 4  
Competition Group  
Riverside House  
2A Southwark Bridge Road  
London SE1 9HA

- A1.5 Note that we do not need a hard copy in addition to an electronic version. Ofcom will acknowledge receipt of responses if they are submitted using the online web form but not otherwise.
- A1.6 It would be helpful if your response could include direct answers to the questions asked in this document, which are listed together at Annex 4. It would also help if you can explain why you hold your views and how Ofcom's proposals would impact on you.

## Further information

- A1.7 If you want to discuss the issues and questions raised in this consultation, or need advice on the appropriate form of response, please contact **Zahid Deen** on 020 7981 3832.

## Confidentiality

- A1.8 We believe it is important for everyone interested in an issue to see the views expressed by consultation respondents. We will therefore usually publish all responses on our website, [www.ofcom.org.uk](http://www.ofcom.org.uk), ideally on receipt. If you think your response should be kept confidential, can you please specify what part or whether all of your response should be kept confidential, and specify why. Please also place such parts in a separate annex.

- A1.9 If someone asks us to keep part or all of a response confidential, we will treat this request seriously and will try to respect this. But sometimes we will need to publish all responses, including those that are marked as confidential, in order to meet legal obligations.
- A1.10 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use. Ofcom's approach on intellectual property rights is explained further on its website at <http://www.ofcom.org.uk/about/accoun/disclaimer/>

## Next steps

- A1.11 Following the end of the consultation period, Ofcom intends to publish a statement in March 2012.
- A1.12 Please note that you can register to receive free mail Updates alerting you to the publications of relevant Ofcom documents. For more details please see: [http://www.ofcom.org.uk/static/subscribe/select\\_list.htm](http://www.ofcom.org.uk/static/subscribe/select_list.htm)

## Ofcom's consultation processes

- A1.13 Ofcom seeks to ensure that responding to a consultation is easy as possible. For more information please see our consultation principles in Annex 2.
- A1.14 If you have any comments or suggestions on how Ofcom conducts its consultations, please call our consultation helpdesk on 020 7981 3003 or e-mail us at [consult@ofcom.org.uk](mailto:consult@ofcom.org.uk). We would particularly welcome thoughts on how Ofcom could more effectively seek the views of those groups or individuals, such as small businesses or particular types of residential consumers, who are less likely to give their opinions through a formal consultation.
- A1.15 If you would like to discuss these issues or Ofcom's consultation processes more generally you can alternatively contact Graham Howell, Secretary to the Corporation, who is Ofcom's consultation champion:

Graham Howell  
Ofcom  
Riverside House  
2a Southwark Bridge Road  
London SE1 9HA

Tel: 020 7981 3601

Email [Graham.Howell@ofcom.org.uk](mailto:Graham.Howell@ofcom.org.uk)

## Annex 2

# Ofcom's consultation principles

A2.1 Ofcom has published the following seven principles that it will follow for each public written consultation:

### Before the consultation

A2.2 Where possible, we will hold informal talks with people and organisations before announcing a big consultation to find out whether we are thinking in the right direction. If we do not have enough time to do this, we will hold an open meeting to explain our proposals shortly after announcing the consultation.

### During the consultation

A2.3 We will be clear about who we are consulting, why, on what questions and for how long.

A2.4 We will make the consultation document as short and simple as possible with a summary of no more than two pages. We will try to make it as easy as possible to give us a written response. If the consultation is complicated, we may provide a shortened Plain English Guide for smaller organisations or individuals who would otherwise not be able to spare the time to share their views.

A2.5 We will consult for up to 10 weeks depending on the potential impact of our proposals.

A2.6 A person within Ofcom will be in charge of making sure we follow our own guidelines and reach out to the largest number of people and organisations interested in the outcome of our decisions. Ofcom's 'Consultation Champion' will also be the main person to contact with views on the way we run our consultations.

A2.7 If we are not able to follow one of these principles, we will explain why.

### After the consultation

A2.8 We think it is important for everyone interested in an issue to see the views of others during a consultation. We would usually publish all the responses we have received on our website. In our statement, we will give reasons for our decisions and will give an account of how the views of those concerned helped shape those decisions.

## Annex 3

# Consultation response cover sheet

- A3.1 In the interests of transparency and good regulatory practice, we will publish all consultation responses in full on our website, [www.ofcom.org.uk](http://www.ofcom.org.uk).
- A3.2 We have produced a coversheet for responses (see below) and would be very grateful if you could send one with your response (this is incorporated into the online web form if you respond in this way). This will speed up our processing of responses, and help to maintain confidentiality where appropriate.
- A3.3 The quality of consultation can be enhanced by publishing responses before the consultation period closes. In particular, this can help those individuals and organisations with limited resources or familiarity with the issues to respond in a more informed way. Therefore Ofcom would encourage respondents to complete their coversheet in a way that allows Ofcom to publish their responses upon receipt, rather than waiting until the consultation period has ended.
- A3.4 We strongly prefer to receive responses via the online web form which incorporates the coversheet. If you are responding via email, post or fax you can download an electronic copy of this coversheet in Word or RTF format from the 'Consultations' section of our website at [www.ofcom.org.uk/consult/](http://www.ofcom.org.uk/consult/).
- A3.5 Please put any parts of your response you consider should be kept confidential in a separate annex to your response and include your reasons why this part of your response should not be published. This can include information such as your personal background and experience. If you want your name, address, other contact details, or job title to remain confidential, please provide them in your coversheet only, so that we don't have to edit your response.

## Cover sheet for response to an Ofcom consultation

### BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

### CONFIDENTIALITY

Please tick below what part of your response you consider is confidential, giving your reasons why

Nothing Name/contact details/job title

Whole response  Organisation

Part of the response  If there is no separate annex, which parts?

If you want part of your response, your name or your organisation not to be published, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

### DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response that Ofcom can publish. However, in supplying this response, I understand that Ofcom may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations. If I have sent my response by email, Ofcom can disregard any standard e-mail text about not disclosing email contents and attachments.

Ofcom seeks to publish responses on receipt. If your response is non-confidential (in whole or in part), and you would prefer us to publish your response only once the consultation has ended, please tick here.

Name

Signed (if hard copy)

## Annex 4

## Consultation questions

A4.1 Our consultation questions are as follows:

*Q4.1 Do you agree that we have identified the correct characteristics of universal service in order to ensure that the universal service remains essentially the same? If not please identify those characteristics that should or should not be specified in the Order, and provide reasons*

*Q4.2. Do you agree we should specify that the duration of redirections, Keepsafe and Poste Restante should be reasonable? If not, please provide your reasons.*

*Q4.3 Do you agree redelivery and return to sender are part of the characteristics of a universal service and should be specified in the order? Please also provide the reasons for your view.*

*Q4.4: Do you agree return to sender should not continue to be required to be provided free of charge? If not please provide your reasons.*

*Q4.5 Do you think the notification period for changes to the list of services provided as part of the universal service should be one month, or three months?*

*Q5.1 Do you agree with a proposed condition to require Royal Mail to provide a universal postal service in line with specified characteristics, which requires them to meet specified standards; requires the provision of access points to particular criteria and which will now also require them to publish a list of universal service products, and to notify us and customers of any changes to that list? If not, please explain why.*

*Q5.2 Do you agree with our proposed condition which specifies universal postal service performance standards? If not, please explain why.*

*Q5.3 Do you agree with our approach to DUSP4 – which means Royal Mail would have to maintain appropriate contingency plans but will have no regulatory requirements in relation to a priority list? If not, please explain why.*

*Q5.4 Do you agree with our proposal to reduce the notice period for price and non-price changes to universal services to one month? If not, please provide evidence to support your view.*

*Q5.5 Do you agree that, given we will now be defining the characteristics of universal services, we should not impose prior approval requirements on Royal Mail for non-price changes to the universal services? If not, please provide evidence to support your view.*

*Q5.6 Do you agree with our proposal not to impose any notification and publication requirements on Royal Mail in respect of retail non-universal services? If not, please provide evidence to support your view.*

*Q6.1 Do you agree with our proposal to delete the requirement in CP 1.2 and the related changes to the PCOPC and Mail Integrity Code? If not, please explain why.*



*Q6.2 Do you agree with our proposed requirement for Royal Mail's compensation arrangements for universal services? If not, please explain why.*

*Q6.3 Do you agree with our proposal to remove CP 3 which requires other RPOs to measure and report on their contract targets? If not, please explain why.*

*Q7.1: Do you agree with the thresholds, timescales and content of notifications under the proposed condition? If not, please provide your reasons.*

*Q7.2: Do you agree with Ofcom's proposed process for handling end-to-end notifications? If not please provide your reasons.*

*Q8.1 Do you agree with our proposed drafting for the Second Class price cap DUSP Condition? If not, please provide your reasons.*

*Q9.1 Do you agree with our proposals for the process for applying for access agreements (and variations to existing agreements); notification and publication requirements; and quality of service requirements? If not, please provide your reasons.*

*Q9.2 Do you agree with the proposals for establishing a USP access condition set out above? If not, please provide your reasons.*

*Q10.1 Do you agree that the new condition and the direction are appropriately set out to capture accurately, completely, and transparently, the regulatory financial reporting requirements we proposed in October consultation (as summarised above)? If not, please provide your reasons.*

*Q11.1 Do you agree with our approach to the cessation of the transitory conditions – and if not, for which specific transitory conditions do you disagree and why?*

## Annex 5

## Proposed conditions and earlier regimes

Table 2: Requirements in licence conditions (prior to general authorisation regime), initial conditions and our proposals

<b>Royal Mail licence condition</b>	<b>Standard licence condition</b>	<b>Initial conditions October 2011</b>	<b>Proposed Conditions<sup>108</sup> April 2012</b>	<b>Regulatory</b>
2	-	DUSP 1	DUSP	
3	-	DUSP 3		
		DUSP 4	DUSP	
4	-	DUSP 5	DUSP	
		CP 1	CP	
		CP 2		
		T 1	delete	
4	2	CP 1.2	delete	
	2	CP 3	delete	
5	-	DUSP 6	Merge with current CP 7-9	
6	-	DUSP 2	Merge with current DUSP1 and 3	
7	-	CP 4	DUSP	
8	3	E 1	E 1	
9	-	USPA 1 and 2	Singular USPA condition	
10	-	USPA 3		
11	5	-	-	
12	6	-	-	
13	-	T 2	delete	
14	4	CP 5	CP	
		T5	delete	
15	-	ACC 1	ACC 1	
16	-	T 3	delete	
17	7	-	-	
18	8	-	-	
19	-	-	-	
20	10	CP 6	CP	
21	-	T 4	delete	
		USPA 4	In singular USPA condition	
22	-	Directions to be issued on the Appointed Day	Directions as made on 1 Oct 2011	
-	9	-	-	
-	11	-	-	
-	-	CP 7-9	CP	
-	-	-	Cap on Second class stamp price in DUSP	
-	-	-	N 1 (notification condition)	

<sup>108</sup> We will make decisions on DUSP and CP condition numbering when we issue our statement.

## Annex 6

# Proposed characteristics of universal services

A6.1 Each universal service product has many attached features and terms and conditions. The table below aims to provide more clarity about what we think is essential to the product currently provided. It summarises the current characteristics of the products provided as part of the universal service which we propose to specify in regulation. In addition, all products are single piece, as highlighted in the main consultation document. However, as in the main consultation document, we welcome any comments on the table and on aspects of the universal service which we may have overlooked.

A6.2 The table lists the characteristics in the left hand side column. In addition to these characteristics, all products in the universal service must also be single piece, and their main function (see below) must be defined. We explain here what most of the terms mean, when it is not straightforward:

- **Definition:** describes what a product does, for instance, a postal service, or a service of redirecting mail.
- **Speed** (sometimes referred to as routing time): the period of time between collection and delivery. More specifically it means the target time for conveyance of a postal packet, from the access point to the delivery point, according to the formula "D + n", where "D" means the deemed date of collection and "n" means the maximum number of working days between that date and delivery.
- **QoS:** Quality of service, expressed in the percentage of letters to be delivered within the specified routing time, when it relates to postal products. Some of the current quality of service relate to the delivery and collection of letters rather than specific products.
- **Customer:** any customer can access these products, regardless of whether they are individual or businesses or where they live.
- **Access points:** access points to universal services. Access points are currently, at a minimum, post boxes (PBs) and post offices (POs). Post boxes are access points for items which can be posted through the post box, otherwise users can go to the post office.
- **Destination:** the geographic area where the product can be delivered or provided. For instance, the First Class service must be available to every address and premises in the UK (except where there are appropriate exceptions: for instance, some addresses are too remote, or mail cannot be delivered in some worldwide destinations).
- **Size:** the dimension of the product.
- **Uniform and affordable:** universal services must be affordable and provided at a uniform price across the UK ("one price goes anywhere"), according to s31 of the Postal Services Act 2011.

- **CoP:** whether Certificate of Posting should be available.
- **Compensation for insurance:** whether compensation is provided in lieu of insurance for a registered or insured product
- **Proof of delivery:** a copy of a signature obtained on delivery of a postal packet.
- **Tracking:** A facility enabling the sender to monitor the progress of a postal packet through the postal network. This facility is only available partially for Recorded Signed For, as customers can only see confirmation of delivery, and for International Signed For, tracking overseas, showing arrival into the country and on delivery in the country, is only available for a limited number of countries.
- **Payment method:** Stamp, meter and PPI. The PPI is an indication on the envelope that the postage has been paid and can be used by customers with an account with Royal Mail. Meter is a way of paying postage in advance, and items have a franking impression made by a franking machine licensed by Royal Mail. Stamps are another way of paying postage in advance, and can be purchased widely in post offices and many other retail outlets. We consider online postage as a subsection of the stamps payment method.
- **Type of items:** the nature or kind of postal packets which can be transported

A6.3 We proposed in the main document that the definition of what a product mainly does should be part of the characteristics. We now define the products in the order by their characteristics (see Annex 6). For cross-reference, we also include below what we consider the main function of the current products provided as part of the universal service:

- **First class, Second class, Standard Parcels:** a service of conveying postal packets
- **Special Delivery Next Day:** registered and insured product
- **International mail:** delivery and collection requirements apply to mail posted outside the UK / onwards transmission to places outside the UK
- **Services for the blind and petition:** free service of conveying postal packets for the blind and partially sighted and free service of conveying an address to the Sovereign or a petition to the Sovereign or Parliament (or the Scottish Parliament, National Assembly for Wales or the Northern Ireland Assembly).
- **International Signed For:** registered and insured product for international mail
- **Recorded Signed For:** add-on delivery service which provides the sender with a signature for First or Second class mailings in the UK
- **Redirections:** a service of redirecting mail from one address to the other
- **Keepsafe:** service which holds customers' mail for a period of time at their local delivery office while they are away, and delivers it on their return
- **Poste Restante:** mail redirected to a chosen post office. Only available for those travelling around and not able to get mail delivered any other way.

A6.4 Key to the table below: SDND = Special Delivery Next Day; ISF = International Signed For; CoP = Certificate of Posting; Id = idem; Av = Available; blank cell = no or not applicable.

A6.5 Although the table below lists the characteristics we consider as essential, the order and related DUSP conditions do not necessarily list all these characteristics product by product in the same way. For instance it is worth noting that:

- The order does not have a sub-category of services matching exactly the list of the current products provided as part of the universal service; instead, it refers to some of the current products within the description of another service. The current Recorded Signed For matches the description of First and Second Class which offer to provide proof of delivery. International Signed For is referenced in the international services. Standard Parcels would be, in the new regulatory framework, one of the services provided as part of the Second Class service.
- Weight of the items does not need to be specified for the first and Second Class service because there is a maximum of 20kg set by the Act.
- Dimensions do not need to be specified as the Act already refers to the UPU dimensions.

**Table 3 - Characteristics of the universal service products**

	First class	Second class	Standard Parcels	SDND	Recorded	Airmail	Surface mail	ISF	Incoming int'al	Redirections	Keepsafe	CoP	Poste Restante	Petitions <sup>109</sup>	Services for the blind <sup>110</sup>
<b>Speed</b>	D+1	D+3	D+3	D+1,1 pm*	First or Second	D+3 EU <sup>111</sup>	Varies	Varies	First class <sup>112</sup>					Un-specified	First / Airmail
<b>QoS</b>	93%	98.5%	90%	99%		85%									
<b>Collection (Mon-Fri)<sup>113</sup></b>	✓	✓	✓	✓	✓	✓	✓	✓		Av <sup>114</sup>	Av	Av	Av	✓	✓
<b>Delivery (Mon-Fri)</b>	✓	✓	✓	✓ <sup>115</sup>	✓	✓	✓	✓	✓	Av	Av	Av	Av	✓	✓
<b>QoS</b>	Delivery and Collection: 99.9% of collection points served each day; 99.9% of delivery routes completed each day; 99.5% of items delivered correctly														
<b>Customer</b>	Any	Any	Any	Any	Any	Any	Any	Any	Any	Any*	Any	Any	Any*	Any	Blind
<b>Access points<sup>116</sup></b>	PBs and POs	PBs and POs	PBs and POs	POs	POs	PBs and POs	PBs and POs	POs	N/A	POs	POs	POs	POs	POs	PBs and POs

<sup>109</sup> Limited information available on Royal Mail's website on petitions

<sup>110</sup> Blind: Blind and partially sighted. Limited information available on Royal Mail's website on services for the blind and partially sighted

<sup>111</sup> D+5 or 7 rest of the world

<sup>112</sup> We understand international mail is treated as First Class mail for delivery in order to meet the European quality of service standards

<sup>113</sup> Monday – Saturday for letters, Monday - Friday for packets

<sup>114</sup> Available 6 days a week to be ordered, at the minimum from post offices

<sup>115</sup> The Saturday service can be purchased for an additional fee. Delivery to some businesses is excluded from the Saturday guarantee (e.g. banks)

<sup>116</sup> access points are for senders, not recipients

Destination	UK	UK	UK	UK*	UK	World	World*	World*	UK	UK*	UK	UK	UK	Gov/Par <sup>117</sup>	UK/world
Size	✓ <sup>118</sup>	✓	✓	✓	✓	✓	✓	✓	✓					✓	✓
Weight	20kg	1kg	20kg	10kg	First or Second	2kg <sup>119</sup>	2kg	2kg	20kg from the EU					1kg <sup>120</sup>	7kg
Uniform affordable	✓	✓	✓	✓	✓	✓	✓	✓	Int'al agreements	✓	✓	✓	✓	✓	✓
Price regulated		Letter stamp										Free	Free	Free	Free
CoP	✓	✓	✓	Proof	Proof	✓	✓	Proof	N/A					✓ <sup>121</sup>	✓ <sup>122</sup>
Compensation / insurance <sup>123</sup>				✓	Some			✓	as per original item						
Proof of delivery				✓	✓			✓	as per original item						

<sup>117</sup> Including the Scottish Parliament, National Assembly for Wales and Northern Ireland Assembly

<sup>118</sup> The Universal Postal Union, a specialised agency of the United Nations, sets the maximum and minimum dimensions of postal packets.

<sup>119</sup> Exceptions apply

<sup>120</sup> This is the weight limit required by the Act in s33(3)(d), although Royal Mail's website states that Royal Mail provides this service up to 2kg, <http://www.royalmail.com/sites/default/files/docs/pdf/Addresses%20and%20Petitions%20December%202010.pdf>

<sup>121</sup> Petitions and services for the blind: unspecified on Royal Mail's website but if they are in fact first or Second Class services Royal Mail is likely to provide CoP where the service is purchased at the post office. To be clarified by this consultation

<sup>122</sup> Petitions and services for the blind: unspecified on Royal Mail's website but if they are in fact first or Second Class services Royal Mail is likely to provide CoP where the service is purchased at the post office. To be clarified by this consultation

<sup>123</sup> Higher level of compensation is provided in lieu of insurance for Special Delivery Next Day and additional compensation can be purchased for International Sign For. Normal (not additional) compensation is provided for Recorded Signed For

<b>Tracking</b>				✓	Partial			Partial	As per original item						
<b>Payment method</b>	All <sup>124</sup>	All	All	Not PPI	All	All	All	All		All	All				
<b>Duration</b>										Up to 2 years	Up to 66 days		Up to 2 months		
<b>Return to Sender</b> <sup>125</sup>	✓	✓	✓	✓	✓	✓	✓	✓	✓						✓
<b>Redelivery</b> <sup>126</sup>	Items that cannot fit within the letter box or must be signed for														
<b>Type of items</b> <sup>127</sup>														Petition/ address	Articles for the blind

\*restrictions apply, e.g. SDND cannot be provided next day by 1pm in some area

<sup>124</sup> Not all payment methods are available for all products, for instance, certain products cannot be paid for on account

<sup>125</sup> Assumed – sender's name and address must be provided for articles for the blind

<sup>126</sup> Includes caller's office – collection from the delivery office – where appropriate

<sup>127</sup> Royal Mail does not carry prohibited or restricted items



## Annex 7

# Regulatory impact assessment for UPSO

## Introduction

- A7.1 The analysis presented in this annex represents an impact assessment, as defined in section 7 of the Communications Act 2003 (the Act).
- A7.2 You should send any comments on this impact assessment to us by the closing date for this consultation. We will consider all comments before deciding whether to implement our proposals.
- A7.3 Impact assessments provide a valuable way of assessing different options for regulation and showing why the preferred option was chosen. They form part of best practice policy-making. This is reflected in section 7 of the Act, which means that generally we have to carry out impact assessments where our proposals would be likely to have a significant effect on businesses or the general public, or when there is a major change in Ofcom's activities. However, as a matter of policy Ofcom is committed to carrying out and publishing impact assessments in relation to the great majority of our policy decisions. For further information about our approach to impact assessments, see the guidelines, Better policy-making: Ofcom's approach to impact assessment, which are on our website:  
[http://www.ofcom.org.uk/consult/policy\\_making/guidelines.pdf](http://www.ofcom.org.uk/consult/policy_making/guidelines.pdf)

## Ofcom's policy objective

- A7.4 Ofcom's overall statutory objective in relation to post, set out by the Postal Services Act 2011 (the Act), is to secure the universal postal service. Accordingly the Act, in s.30, requires us to provide a description of the universal services, and the standards with which they must comply, by order. The first Universal Postal Service order implements the requirement in s.30. Currently, the obligation on Royal Mail to provide the universal service is set out mainly by a list of names of products. To move to a description of the services as required by the Act, we propose to move to a description of the characteristics of the products, rather than a list of names.
- A7.5 Under s.30, before making or modifying a universal service order, Ofcom must review the extent to which the market for the provision of postal services meets the reasonable needs of postal users (we refer to this work as the review of user needs). This requirement does not apply to the first UPSO, but such a review must be conducted within 18 months of vesting (so before 1 April 2013). Ofcom is consulting on the first universal service order in the review of regulatory conditions of which this impact assessment is an annex, with a view to it coming into force from 31 March 2012. It is therefore possible that this first order would be in place for about a year, depending on the outcome of the review of user needs.

## The citizen and/or consumer interest

- A7.6 The universal postal service is the collection and delivery of postal packets at an affordable uniform price, everywhere in the UK, six days a week (five for packets). The universal postal service ensures that everyone in the UK is able to communicate by post, by requiring a collection and delivery of post every working day. It promotes social cohesion and helps economic and commercial transactions.

As stated by Richard Hooper in its 2008 report to review the UK postal services sector<sup>128</sup>: “*The ability to deliver items to all 28 million business and residential addresses in the UK is part of our economic and social glue.*”

## Options considered

A7.7 There are three options:

- **Option 1:** not to make an order. In practice this would mean that we would keep the current list of services in the conditions imposed on the Universal Service Provider.
- **Option 2:** to make an order describing the essential features of the current universal service. This would include the characteristics as defined in the Section below.
- **Option 3:** to make an order describing the universal service while also substantively changing the current universal service.

## Analysis of the different options

### Option 1- Not to make an order

A7.8 We consider that not making an order describing the universal service is not a feasible option. We have a clear obligation under s.30 of the Act to set out by order a description of the universal services and the standards with which they must comply.

A7.9 The Act does not set a time limit for the introduction of the first order. However, we consider that the policy intention was clearly that Ofcom would make an order at the first opportunity, given s.30(4) envisages that Ofcom would make the first order without having had the opportunity to carry out a review of postal user needs. Because of the transitional arrangements in schedule 9 (paragraph 5(4)), making the first order will result in the revocation of the transitory conditions. Therefore it makes sense to implement the order at the same time as we implement the new regulatory framework.

### Option 2 - To make an order describing the essential features of the current universal service

A7.10 Currently the universal service is secured by requiring Royal Mail to provide it, mostly through a list of services in regulatory condition DUSP 1, formerly licence condition 2 of Royal Mail’s licence. Moving towards a description-based universal service would mean that Ofcom would stop requiring Royal Mail to provide named services as part of the universal service and instead require Royal Mail to provide the universal service in a way that meets the characteristics defined by Ofcom in the order.

A7.11 However, in proposing the change to a description of services under this option, we intend to retain all the essential features of the universal service.

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<sup>128</sup> Richard Hooper CBE, Dame Deirdre Hutton, Ian R Smith, *Modernise or decline – Policies to maintain the universal postal service in the United Kingdom*, December 2008, <http://www.bis.gov.uk/files/file49389.pdf>

A7.12 In summary we propose that the following characteristics should be specified:

- **Definition of the product.** This is to describe what a product mainly does, for instance, a postal service, or a service of redirecting mail.
- **Delivery and collections six days a week for letters, five for packets.** This is a minimum requirement of the Act.
- **Universal access.** This requires that any customer may send items or access the service from access points (post boxes and post offices for packets and registered items, post boxes for letters), to every home and premises in the UK (or worldwide)<sup>129</sup>. This is a minimum requirement of the Act.
- **Uniform and affordable prices.** While we have proposed in the October consultation to give Royal Mail commercial freedom in setting prices for universal service products (with the exception of the price cap for Second Class stamps for standard letters), the prices for these products must be (a) the same regardless of destination within the UK (i.e. uniform) and (b) affordable. This is a minimum requirement of the Act.
- **Single piece, where applicable** (in effect excluding products attracting presentation and volume discounts). For the purpose of the order, we consider that a single piece service means a postal service whose price (on average for each postal packet) is not subject to any discounts related to number of postal packets sent in connection with the person who paid for the service, the positioning of text on the postal packet, the use of markings which facilitate the use of machines to sort postal packets or the pre-sortation into geographical areas for delivery<sup>130</sup>.
- **Speed and associated quality of service targets.** We consider that this is a key characteristic of the products. This would include, for instance, the guaranteed delivery by 1pm of Special Delivery Next Day.
- **Dimensions and weight.** These are specified by the UPU<sup>131</sup> and the Act<sup>132</sup>.
- **Tracking.** Although it could be argued this is a commercial add-on to Special Delivery Next Day, it is currently an integral part of the service. We do not however propose to specify tracking for Recorded Signed For and International Signed For, which only have a partial tracking facility.

A7.13 This covers the characteristics of postal services we identified as most important to the delivery of the universal service. Because we seek to preserve the essential characteristics of the universal service, we identified these characteristics by

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<sup>129</sup> Services for the blind would of course only be available to the blind.

<sup>130</sup> This definition is based on the Postcomm definition of single piece expressed in its August decision on the universal service, with the following exceptions. The Postcomm definition excluded premium products (e.g. Recorded Signed For) from the definition, whereas we do not make this distinction. In addition, it excluded discounts related to payment channel whereas Ofcom's definition does not. Source: Postcomm, *Removing bulk products from the universal service and clarifying the status of other universal service products – a decision document*, August 2011

<sup>131</sup> section 33(1)(b) of the Act

<sup>132</sup> section 33(1)(a) of the Act

considering the requirements of the Directive and the Act and the current product description and terms and conditions. Annex 6 includes further details about the characteristics associated with the products currently provided as part of the universal service, Annex 9 includes a draft order and Annex 10 includes associated conditions.

A7.14 We propose that Royal Mail's universal service products must match the characteristics we specify, but in order to provide commercial flexibility, their products need not be limited to these characteristics. In other words, it may be that their products, while meeting the essential features of the universal services, also have additional features.

A7.15 The characteristics which we propose not to specify are:

- **Price.** The specific prices are an issue discussed in our October consultation (focused on securing the provision of the universal service – it includes proposals to lift price controls but with a safeguard for vulnerable consumers via a price cap on Second Class stamped letters). An exception is where the Act requires certain services to be provided free (for instance, services to the blind) or the same is true of the existing universal service as set out in condition DUSP 1 (for example, certificate of posting). We will specify that universal services must have a uniform and affordable price.
- **Format of the items** i.e. letter, large letter and parcels, or *weight steps*. Royal Mail sets prices according to these formats. Therefore, to define format would be to intervene on pricing, whereas in the October consultation we are proposing that Royal Mail should have commercial freedom to set prices (with the exception of the price for Second class stamps for standard letters). This does not relate to maximum weight or dimensions (e.g. length), which we will specify in line with the requirements of the Act and the UPU.
- **Requirements imposed on customers.** This is what Royal Mail asks of its customers when it performs the services, such as requiring a return address on Airmail envelopes, or specifying that the guarantee of Special Delivery Next Day does not apply if no-one is at the address. These seem to relate to operational and practical issues which do not appear to require regulation. There are some rare exceptions where we need to specify some of those requirements as part of the regulatory instruments, e.g. in relation to petitions, where unless we specify the presentation requirements the obligation may be drawn more widely than it is intended to.

A7.16 In addition, we propose not to include the following features in the universal service products characteristics, because they can already be required in other regulatory conditions:

- **Compensation.** We believe the availability of compensation is important but we consider the issue of compensation separately, in Section 6 of the consultation document, as part of Consumer Protection conditions. We propose to require the provision of reasonable compensation, where this is currently provided by Royal Mail for universal service products<sup>133</sup>.

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<sup>133</sup> By compensation here we mean “normal” compensation, other than the compensation required for insured and registered services. In respect of these services we propose to require a domestic and a

- **Times of collection and delivery.** Times of collection and delivery have not previously been regulated directly as part of the universal service. DUSP 5.3 requires Royal Mail to notify us of the specified delivery and collection times from post boxes, any changes they intend to make to those times, and any reclassification which results in the collection time starting earlier. We propose to keep this notification requirement, as evidence suggests that times of delivery and collection, and in particular consistency of delivery times, are important to customers<sup>134</sup>.

A7.17 Arguments in favour of option 2 are:

- **Act requirement.** Ofcom needs to comply with the requirement of the Postal Services Act 2011 to provide a description of the universal services, and the standards with which they must comply, by order. Currently, there could arguably be some debate about the characteristics of the products and the terms and conditions which should be part of the product definition. These are not set out clearly in regulation, but instead are linked to the description of Royal Mail's products given by Royal Mail on its website.
- **No substantive change to the essential features of the universal service.** With this option we intend to maintain the essential features of the universal service as they currently are, and we consider that customers will see little difference in practice. This is not to say that, from time to time, Royal Mail cannot make changes to some of the terms and conditions relating to universal service products. Such certainty is also important for regulatory purposes (e.g. the future regulatory monitoring of Royal Mail). This fulfils our commitment in our proposals for the future framework for economic regulation that "*the scope of the universal service will remain unchanged from the present scope*", pending the review of user needs<sup>135</sup> and its implications, if any, for the universal service. The minimum requirements of the universal service cannot, in any event, be changed without approval from Parliament.
- **Customer protection.** The current list-based approach to providing more details about the composition of the universal service was sufficient to protect customers when Royal Mail needed approval to change non-beneficial terms and conditions. However, we are also proposing to move away from the approval mechanism and we therefore need to be clearer about the characteristics of the products which are essential to preserve to maintain the current universal service. Customers will know the features of the universal service for which they can expect regulatory safeguards.
- **Clarity.** Currently, because the products within the universal service are defined by giving the name of the product, the definition of each product is not necessarily systematic or complete, and relies on the definition given by Royal Mail. This will clarify the characteristics necessary for Royal Mail to meet in order

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cross-border insured and registered service(s) to be provided, in accordance with the Postal Services Directive and s.32 of the Act.

<sup>134</sup>See for instance Jigsaw Research, *Postcomm Customer Survey 2008*, February 2009, <http://stakeholders.ofcom.org.uk/binaries/post/93.pdf>. For instance, SMEs surveyed were resistant to later delivery times,

<sup>135</sup>Our work on reviewing the needs of postal users must be completed by April 2013 and we consider it appropriate to retain essentially the same service until then.

to fulfil its universal service obligation. Such clarity is beneficial to postal users, who will be able to refer to the characteristics to know what to expect of universal service products.

- **Focus.** This allows us and all interested parties the opportunity to consider the characteristics of the universal services and specify the ones which must be provided to meet the minimum requirements and which are necessary to reflect the current universal service products.
- **Flexibility.** In future, this move will allow us to move away from considering the universal service as a suite of products, towards identifying the characteristics which are important to customers. While retaining the current features of the universal service, this could give Royal Mail some limited flexibility to consider product terms and conditions where this is not essential to the current universal service. It paves the way for a more flexible approach to the composition of the universal service in future, should this become desirable.

A7.18 As noted above we intend to ensure that the universal service remains essentially the same following the introduction of the first UPSO and new DUSP. In particular, we think this will be achieved by our approach of describing the essential characteristics of the services. If stakeholders consider that there are important characteristics of the universal service that we have not captured in our descriptions, this consultation is the opportunity to bring this to our attention.

A7.19 Furthermore, in those areas where we are proposing Royal Mail should have greater commercial freedom regarding non-price terms and conditions for universal service products, we are proposing that all such terms are fair and reasonable. We are also proposing that Royal Mail must give one month's notice before changing prices or non-price terms and conditions for universal service products.

### **Option 3 - To make an order describing, but also substantively changing, the universal service**

A7.20 As described above this option would require Royal Mail to provide products which meet the characteristics defined by Ofcom in the order. However, under this option, we would not seek to preserve the essential features of the current universal service. We could, for instance, describe the universal service with less attributes, such as retaining solely the minimum requirements of the Act, allowing the maximum commercial flexibility to Royal Mail. Alternatively, we could describe the service in such a way that it would require changes to the list of services currently provided as part of the universal service, or changes to these services.

A7.21 We consider that we should carry out the review of user needs first, as a review of user needs will enable us to gather evidence as to whether the reasonable needs of users are met, and to make informed decisions. The Act clearly envisages that, ordinarily, Ofcom would conduct a review of user needs before making or modifying a UPSO. This does not apply to the first order, but Ofcom must carry out such a review within 18 months (we refer to it as the review of user needs). Therefore it is more appropriate to carry out the review of user needs before substantial changes, if any, to the universal service.

A7.22 The argument in favour of this option is that some stakeholders have previously argued that the current universal service needs to be reviewed. The risk of this option is that we would change the universal service without current evidence on whether the reasonable needs of postal users are met, and therefore fail to ensure

that the universal service meets their reasonable needs. This risk can only be mitigated to a limited extent by relying on past evidence, such as the research commissioned by Postcomm and Consumer Focus on the needs of users from the universal service<sup>136</sup>, as prior evidence only covers specific aspects of the universal service.

## Assessment

A7.23 **Option 1** would have the following impact:

- There would be no change from the status quo;
- Ofcom would not fulfil its statutory obligation until the user needs review had been completed;
- Royal Mail itself, users and competitors would face uncertainty about what the universal service comprised; and
- The universal service would be likely to comprise all the terms and conditions of the listed products, as of 1 October 2011, and would therefore be as restrictive as is possible of Royal Mail.

A7.24 **Option 2** would have the following impact:

- The universal service remains essentially the same for customers. They would benefit from the possibility of beneficial minor changes to the products until the review of user needs;
- Royal Mail would benefit from some more flexibility to change some product terms without prior approval. It would retain the obligation to provide the essential characteristics of the current universal service; and
- The impact on competitors is likely to be neutral - as our proposals are of more interest to customers, and the universal service remains essentially the same.

A7.25 In addition, it is difficult to anticipate all changes that Royal Mail may seek to make to the terms and conditions of the products provided as part of the universal service. We consider that the non-price terms of universal services should be fair and reasonable. The recent applications from Royal Mail provide examples of the type of issues that could arise, such as a change to the retention period of undeliverable items, or Royal Mail's trial of the delivery of postal items to a neighbour where they cannot be delivered to an absent addressee because a signature is required or the item is too big to put through the letterbox<sup>137</sup>. In these instances, where we consider that there is a justifiable case for doing so, we can assess whether the proposed terms are fair and reasonable.

A7.26 **Option 3** would have the following impact:

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<sup>136</sup> TNS-BMRB, *Residential customer needs from a sustainable universal postal service in the UK*, November 2010, <http://stakeholders.ofcom.org.uk/binaries/post/1183.pdf> and the report on business customer needs, <http://stakeholders.ofcom.org.uk/binaries/post/1184.pdf>

<sup>137</sup> Postcomm, *Royal Mail Terms and Conditions Consultation Decision*, September 2011, <http://www.psc.gov.uk/consultations/royalmailstermsandconditions/decision>

- A review of user needs has not been undertaken yet so it would not be sufficiently clear as to whether changes meet the reasonable needs of users, and therefore it would be difficult to assess the impact on customers. There would be a risk of significant detriment to users; and
- The impact on Royal Mail and competitors would depend on the specific proposals we made.

## The preferred option

A7.27 Ofcom's preferred option is option 2, to move towards a description-based universal service. We consider that:

- This is the only option that fulfils our statutory requirement to describe the services to be provided as part of the universal service, and the standards with which they must comply; and
- We should maintain the essential features of the universal service pending the conclusion of the review of postal user needs.

## Duration periods for Redirections, Keepsafe and Poste Restante

### Ofcom's policy objective

A7.28 As part of our consultation on the order we are consulting on the duration periods for Redirections, Keepsafe and Poste Restante. We aim to provide a description of the essential features of the universal services, here Redirections, Keepsafe and Poste Restante. Our objective is to preserve what is important about the current universal service while making sure that Royal Mail can make appropriate changes if necessary.

### The citizen and/or consumer interest

A7.29 These products were included in the universal service to protect mail integrity and security.

## Options

A7.30 There are two options:

- Option 1: to replicate in regulation the current duration periods
- Option 2: to require "reasonable" duration for these products.

## Analysis of the different options

### To replicate in regulation the current duration periods

A7.31 Redirections, Keepsafe and Poste Restante are all services which can be requested from Royal Mail for a specific period of time, rather than being a "one-off" service. We consider that the fact that these products are available for a period of time is an essential characteristic of the products: the value of the Redirection service relies on the fact that mail can be redirected over a certain period.



A7.32 The current duration periods of these products are:

- *Redirections*: for periods of one month, three months, six months and 12 months, with the ability to renew redirection services for up to a maximum of two years from the commencement of the initial redirection service
- *Keepsafe*: for any periods up to 66 days
- *Poste Restante*: 14 days if the item was posted in the UK (including the Channel Islands and the Isle of Man), one month if it was posted overseas, two months if it is addressed to a post office branch at a sea port if the customer is arriving by ship.

A7.33 Argument in favour of option 1 is that it would guarantee no change to the current situation (unless the regulations are changed).

A7.34 However the risk would be that Royal Mail would not be able to change the duration offered at all until and unless we made a change to the regulatory framework. This would set the current durations in stone for the near future and only replicates the status quo of today – when it is possible that Royal Mail may want to make minor changes which do not have a detrimental impact on customers or are of benefit to customers.

A7.35 We therefore consider that the impact would be negative for both Royal Mail and customers, and neutral for competitors which do not currently compete for this product.

### **To require “reasonable” duration for these products**

A7.36 Arguments in favour of option 2 are:

- customers continue to enjoy the service, as a reasonable period for the service must continue to be provided by Royal Mail;
- allowing some changes to the period of time the service is currently offered, if necessary.

A7.37 The risk would be that Royal Mail could make non-beneficial changes to the duration period of these products. However, as outlined above, this risk is mitigated by our proposal to require that the non-price terms and conditions for universal service products are fair and reasonable, and our proposal to require one-month notification of non-price changes to universal service products, and to require Royal Mail to publish a list of universal services, to be updated if there is a change.

A7.38 We therefore consider that the impact would be negative for both Royal Mail and customers, and neutral for competitors which do not currently compete for this product.

### **The preferred option**

A7.39 Ofcom’s preferred option is option 2, to require “reasonable” duration for these products. We consider this option would best balance our objectives of preserving what is important about the current universal service without preventing Royal Mail from making appropriate changes if necessary.

A7.40 Redelivery, caller's service and return to sender

## Ofcom's policy objective

A7.41 As part of our consultation on the order we are consulting on whether to include redelivery, caller's service and return to sender in regulations. We aim to provide a description of the essential features of the universal services. Our objective is to preserve what is important about the current universal service while making sure that Royal Mail can make appropriate changes if necessary.

## The citizen and/or consumer interest

A7.42 The universal postal service ensures that everyone in the UK is able to communicate by post, by requiring a collection and delivery of post every working day at an affordable, uniform price. Sometimes however, the recipient is not at home to receive a packet which cannot be posted through the letter box or needs to be signed. In these cases, we consider that it is important for the integrity of mail and for customers' protection that there is a reasonable attempt to reach the sender or recipient.

## Options

A7.43 Royal Mail's redelivery service for parcels, Special Delivery Next Day and Recorded Signed For means that a packet can be delivered to a local post office for collection by the customer, redelivered to another address within the same postcode, or redelivered another day to the original address. Collection from the delivery office ("caller's service"<sup>138</sup>) is also available. Redelivery and collection from the delivery office are not currently mandatory for Royal Mail to provide. While redelivery and caller's service are two distinct activities, for the purposes of this Section, we include caller's service in redelivery.

A7.44 The return to sender service is the service whereby the customer receives a letter with the correct address but the wrong name, writes "return to sender" or "not known at this address" and puts it back in a pillar box or post office. Royal Mail then, where it is able to identify the sender, delivers it back to the sender<sup>139</sup>. Return to sender is currently required to be provided free of charge as part of a regulated product in transitory condition, T 4.

A7.45 Neither redelivery nor return to sender will be required to be provided in the new regime if we do not actively decide that they are part of the terms of a universal service and therefore should be provided.

A7.46 There are two options:

- **Option 1:** not to require in the order that redelivery and return to sender should be provided

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<sup>138</sup> See Royal Mail's website for more information:

<http://www.royalmail.com/sites/default/files/docs/pdf/Callers%20Service%20Web%20December%2010.pdf>

<sup>139</sup> For more information on how Royal Mail deals with items which need to be returned see <http://www2.royalmail.com/customer-service/safe-and-sound>, <http://www2.royalmail.com/customer-service/getting-other-peoples-mail> and <http://www2.royalmail.com/customer-service/personal-customers/missed-deliveries/what-happens-dont-pick-item>

- **Option 2:** to require in the order that redelivery and return to sender should be provided.

## Analysis of the different options

### Option 1 - Not to require in the order that redelivery and return to sender should be provided

A7.47 Arguments in favour of option 1:

- It could be argued that the postal service is provided at the first attempt at delivery to the address, and everything else is additional – in which case redelivery or return to sender are not components of the current universal service products.
- Such terms and conditions related to Royal Mail's products should not be regulated to preserve Royal Mail's commercial flexibility.

### Option 2 - To require in the order that redelivery and return to sender should be provided

A7.48 Arguments in favour of option 2:

- It could be argued that delivery implies that the item has been transferred to the intended address, and that this is not achieved if there has not been some reasonable effort to ensure that the item reaches the addressee<sup>140</sup>. By reasonable effort, we mean one attempt at redelivery or collection by the customer. Royal Mail's current practice, and that of other parcel operators, seems to point in that direction.
- We consider that redelivery is an important aspect of the service for customers in that it enables those not available at the time of delivery to obtain their item.
- it is reasonable to expect Royal Mail to return the item to the original sender, who paid for the service, if the item is returned in the post. This does not impose an obligation on Royal Mail to return the item to the sender if Royal Mail introduces a choice for some products and the sender chooses not to have the item returned.

A7.49 There is a risk that this constrains Royal Mail's commercial flexibility further than is currently the case. We consider that this does not impose additional regulatory requirements on Royal Mail, as Royal Mail currently needs prior approval of all non-price non-beneficial changes. In addition, Royal Mail will continue to be able to adapt to customer needs: the only thing required is one attempt at delivery and collection and one attempt at returning to sender, in the same way as Royal Mail currently provides it. Our proposal only applies to redelivery and return to sender of items sent by using a universal service (such as, currently, First class).

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<sup>140</sup>The Postal Services Directive replaced the term "delivery" by "distribution" in defining postal services. Distribution is defined as "the process from sorting at the distribution centre to the delivery of postal items to their addressees".

A7.50 In line with our proposals in October to provide Royal Mail with more flexibility<sup>141</sup>, we are not proposing to continue to require return to sender to be free of charge. This implies that Royal Mail could require payment by the sender even though they did not seek this service, although of course, if return to sender is considered part of the universal service (following our consultation) the terms and conditions should continue to be fair and reasonable, and we will continue to monitor the provision of the universal service products. Alternatively for items purchased at the post office, Royal Mail could introduce a specific, opt-in service<sup>142</sup>. In relation to the price terms under these scenarios, as set out in our October consultation, our proposal to grant Royal Mail's commercial freedom will be subject to regulatory safeguards, in particular effective monitoring of performance.

### The preferred option

A7.51 Ofcom's preferred option is option 2, to require redelivery, caller's service and return to sender. We consider this option would best balance our objectives of preserving what is important about the current universal service without preventing Royal Mail from making appropriate changes if necessary.

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<sup>141</sup><http://stakeholders.ofcom.org.uk/binaries/consultations/securing-the-postal-service/summary/condoc.pdf>

<sup>142</sup> Royal Mail's current terms and conditions for undeliverable and re-posted letters can be found in the Inland Letter Post Scheme, <http://www.royalmail.com/sites/default/files/docs/pdf/ILPScheme.pdf>.

## Annex 8

## Regulatory Accounting appendix

- A8.1 This Appendix is for illustration purposes; only to enable the reader to gain an overview of the requirements set out in the draft Condition and Direction (including the RAG).
- A8.2 For the avoidance of doubt, in the event of any difference between the information set out below and the information in the draft Condition and Direction, the information in the draft Condition and Direction takes precedence.
- A8.3 The reporting and disclosure requirements for the regulatory financial statements and other regulatory financial reports to be produced by Royal Mail for the 2012-13 financial year onwards are set out in the tables below. Annual reports are to be provided within four months of year-end and quarterly reports within three months of quarter-end.

Table 4: Information required for the Relevant Group

Entity	Requirement	RAG Reference	Frequency	New	Audit	Publish
<b>Relevant Group</b>	Consolidated income statement	Figure 1	Annual	Yes	Yes	Publish
	Consolidated balance sheet statement	Figure 2	Annual	Yes	Yes	Publish
	Consolidated cash flow statement	Figure 3	Annual	Yes	Yes	Publish
	Consolidated quarterly cash flow projection statement	Figure 4	Quarterly & Annual	Yes	No	No
	Strategic Business Plan	Paragraph 1.13	Annual	Yes	No	No
	Reconciliation of consolidated income, balance sheet and cash flow statements with the consolidated accounts of RMH plc	Figures 1,2 and 3	Annual	Yes	Yes	Publish

**Table 5: Information required for the Reported Business**

Entity	Requirement	RAG Reference	Frequency	New	Audit	Publish
<b>Reported Business</b>	Annual Income statement (to EBIT only)	Figure 5	Annual	No	Yes	Yes
	Quarterly Income statement (to EBIT only)	Figure 5	Quarterly	No	No	Yes
	Quarterly reconciliation of income statement (to EBIT only)	Paragraph 1.18	Annual	No	Yes	Yes
	Annual reconciliation of income statement (to EBIT only)	Figure 7	Annual	No	Yes	Yes
	Annual balance sheet statement	Figure 8	Annual	No	Yes	Yes
	Annual reconciliation of balance sheet statement	Figure 9	Annual	No	Yes	Yes
	Annual cash flow sheet statement	Figure 10	Annual	No	Yes	Yes
	Annual reconciliation of cash flow sheet statement	Figure 11	Annual	No	Yes	Yes

**Table 6: Information required for the “Four FRE’s” within the Reported Business**

Entity	Requirement	RAG Reference	Frequency	New	Audit	Publish
<b>Reported Business - Separated</b>	Annual Income statement - separated (to EBIT only)	Figure 5	Annual	Yes	Yes	Yes
	Quarterly Income statement - separated (to EBIT only)	Figure 5	Quarterly	Yes	No	Yes
	Quarterly reconciliation of income statement - separated (to EBIT only)	Paragraph 1.22	Quarterly	Yes	No	Yes
	Annual extended end to end Income statement for USO <sup>143</sup> , non-USO and non-Mails (to EBIT only)	Figure 6	Annual	No	Yes	Yes
	Quarterly extended end to end Income statement for USO, non-USO and non-Mails (to EBIT only)	Figure 6	Quarterly	Yes	No	Yes
	Annual balance sheet statement - separated	Figure 8	Annual	Yes	Yes	Yes
	Annual cash flow sheet statement - separated	Figure 10	Annual	Yes	Yes	Yes
	Annual product profitability statements	Figure 12	Annual	No	Yes	No except access
	Quarterly product profitability statements	Figure 12	Quarterly	No	No	No

<sup>143</sup> USO – is shorthand for universal service in this table.

Entity	Requirement	RAG Reference	Frequency	New	Audit	Publish
	Monthly revenue, cost and volume information statements	Figure 13	Monthly	No	No	No

- A8.4 Royal Mail should prepare full accounts (income statement, balance sheet, and cash flow statement) for the Relevant Group along with quarterly cash flow projections for the subsequent two years.
- A8.5 The income statement requirement to EBIT level for the Reported Business and the Four FREs is in principal the same as that produced by Royal Mail for 2011-12, although for 2012-13 there is an additional requirement to show separately details of transfer charging for revenue and expenditure.
- A8.6 The Balance Sheets for the Reported Business and the Four FREs must show detail of their respective assets and liabilities, in so far as they relate to the operational trading activities.
- A8.7 Long term liabilities and assets of the Relevant Group outside of those associated with the operational trading activities of the Reported Business are excluded from the statements of the Reported Business, but form part of the reconciliation to the full Relevant Group accounts.
- A8.8 The Product Profitability Statements are of similar form to those previously produced by Royal Mail for regulatory financial reporting purposes.