



ROYAL MAIL ACCESS PRICING REVIEW

– Proposed Amendments to the Regulatory Framework

Response from Secured Mail

The comments made in this response may be published and attributed to Secured Mail.

1. Summary:

- 1.1 Secured Mail believes competition in the UK mail market has brought significant benefits to mail users, as well as providing a useful stimulus to efficiency improvement by Royal Mail, and strongly supports the development of effective competition in the UK market.
- 1.2 Secured Mail does not itself deliver mail to the delivery address, instead using downstream access. It believes competition using access in this way is an important form of competition, as is E2E (final delivery) competition, and it is important for Ofcom to address the needs of access users as well as seeking to promote E2E competition, not least as E2E competition will always need to use access for final delivery of some mail.
- 1.3 Secured Mail agrees with Ofcom's decision that E2E competition does not currently jeopardise Royal Mail's provision of the universal service, and so there is not currently a conflict between Ofcom's Competition Act and Postal Services Act duties.
- 1.4 Secured Mail does not seek to challenge Ofcom's analysis of the case for intervening in future access and agrees with the intent of the Ofcom proposals, including that there is a need to set conditions on Royal Mail which will encourage improved efficiency. However, Secured Mail's has some concerns at some of the detailed aspects of Ofcom's proposals.
- 1.5 The main concern of Secured Mail is that the proposals may be too narrowly focused on Royal Mail's zonal access pricing (aimed at supporting development of E2E competition). Given the benefits from access competition in general, Secured Mail believes Ofcom should consider more fully the needs of access users in general, in particular that there is a clear objective to see improved efficiency by Royal Mail.
- 1.6 Part of Ofcom's Postal Services Act duty regarding universal service provision is for that provision to be efficient before the end of a reasonable period of time. Secured Mail questions whether the proposals are enough to achieve that outcome. Hence, in our view, Ofcom may need to consider additional requirements on Royal Mail for efficiency improvement.
- 1.7 Secured Mail also believes Ofcom must continue to monitor the sustainability of universal service provision by Royal Mail, as well as how efficient that provision is.

2. Response to Ofcom Questions:

Q1: Do you agree with Ofcom's analysis of the case for intervening as proposed in this section?

- 2.1 Secured Mail notes Ofcom's assessment of its duties under the Competition Act and the Postal Services Act and does not disagree with the conclusion that provision of the universal service is not currently under threat, and does not seek to challenge Ofcom's analysis of the case for intervening in future access pricing.
- 2.2 We also do not disagree with Ofcom's view that, if it does not act now to reduce the risks to development of E2E competition, it is possible such competition will provide an important incentive on Royal Mail to continue efficiency improvement in access and other mail services more generally, to the detriment of all mail users.
- 2.3 In common with Ofcom, Secured Mail sees risk that lack of sufficient pressure on Royal Mail efficiency could lead to excessive pricing and that current freedom in access pricing can mean large price increases, which cause damaging uncertainty for mail users and mail operators.
- 2.4 Secured Mail strongly supports the need for effective competition, including thorough downstream access. Effective competition requires an efficient Royal Mail and we believe that Royal Mail can and needs to become more efficient, we therefore support Ofcom's view that it needs to act now to encourage such improvement.
- 2.5 Ofcom believes that the development of E2E competition is necessary to address the concerns it has set out. Secured Mail does not disagree, but as an E2E competitor will always need to use access for delivery of some of its mail, we believe Ofcom may wrongly be focusing too narrowly on proposals to address the risks identified for E2E competition, without also considering means to improve the position for all access users and ensure sufficient encouragement for efficiency improvement.
- 2.6 Secured Mail notes that Ofcom's assessment of there being no conflict between its Competition Act and Postal Services Act duties is based on the current position and is not certain to be so in future years. It is, therefore important that Ofcom remains watchful and ready to act if the position changes.

Q 2: Do you agree that the options of doing nothing and of imposing a price control on the level of Royal Mail's prices are not appropriate or proportionate?

- 2.7 Ofcom see four options to address the concerns and risks it identifies:
 - a) Rely on existing regulation
 - b) New retail price controls
 - c) New access price controls
 - d) Limits on access pricing freedom
- 2.8 Secured Mail agrees with Ofcom that options a) and b) will not address the issues and will not achieve the necessary Royal Mail efficiency improvement.
- 2.9 Ofcom has decided against option c) because, it believes, that option will not allow Royal Mail enough pricing freedom to respond to E2E competition and because it sees practical difficulties with that option. However, Ofcom seems only to have considered minimum or maximum wholesale price controls and Secured Mail notes that Ofcom does use wholesale price controls for some BT prices, where Ofcom must believe they are effective and workable.

- 2.10 Secured Mail believes that Ofcom should consider a wholesale price control which applied to all access prices and which limited increases in access prices (rather than setting minimum or maximum prices) and so provided direct pressure on Royal Mail to improve efficiency.
- 2.11 Ofcom might also consider setting efficiency improvement targets for Royal Mail (with a timetable to achieve appropriate efficiency within a reasonable period of time) and so directly address the Postal Services Act duty.

Q 3: Do you agree with our approach to focus on existing Royal Mail zones to develop our response to the threats to end-to-end competition? If not, please set out your reasons?

- 2.12 The scale of E2E competition is currently very low and (other than Whistl, who offer only 3-days-a-week delivery) Secured Mail doesn't know of any large E2E entrant. So it is possible E2E competition will not offer a wide enough range of service specifications to provide real choice for mail users.
- 2.13 Similarly, there is very low usage of Zonal access (which is the focus of Ofcom's proposals) while most access use, including by the many of the large mail users who have their own access contracts, is national access.
- 2.14 By focussing on the interests of E2E competitors and zonal access, we believe it is possible that the needs and concerns of access users in general are not properly addressed by Ofcom's proposals.
- 2.15 As mentioned above, we therefore believe that Ofcom should consider other conditions on Royal Mail, such as a general access price control or a direct efficiency improvement target.

Q 4: Is our proposed approach to the definition of 'Zones' appropriate?

- 2.16 Secured Mail does not disagree with Ofcom's approach to the definition of Zones.
- 2.17 It is important to have a process which allows Royal Mail to change its zonal structure, to respond to changes in the market, but appropriate to have the safeguard of Royal Mail doing so through Ofcom as general freedom for Royal Mail to make changes would significantly increase uncertainty for access users.

Q 5: Do you agree with our proposals regarding Zonal charges to address our competition concerns? If not, please explain why.

- 2.18 Secured Mail does not disagree with the principle of requiring the ratio of Zonal Access prices to follow the ratio of zonal access costs.
- 2.19 However, it may be appropriate to allow Royal Mail some flexibility from exactly replicating the ratio of zonal costs in zonal prices, if that encourages efficient competition and does not allow improper anti-competitive action by Royal Mail.
- 2.20 Secured Mail favours using LRIC rather than FAC for zonal costs, as using LRIC should mean lower access charges for all access users. As Ofcom has concerns about the robustness of the LRIC costing model at the moment, it may be necessary to use FAC costs until Ofcom has the necessary confidence on the LRIC model.

2.21 Ofcom believes that it would not be consistent with the zonal pricing rule for Royal Mail to offer volume discounts or discounts based on having a general geographic profile of access mail. Secured Mail does not disagree, but believes that if Royal Mail can evidence lower costs where an access customer accepts and keeps to clear requirements (e.g. committing to a stated volume of mail), discounts could be justified and permitted, provided such discounts were available to all access users (national and zonal).

Q 6: Do you agree with the proposed weighted average rule? If not, please explain why.

2.22 Secured Mail does not disagree with Ofcom's proposals on the weighted average rule.

Q 7: Do you agree with our assessment of and proposed approach towards tolerances and profile surcharges on national contracts? If not what alternative would you propose?

2.23 Secured Mail does not disagree with Ofcom's assessment and proposals regarding tolerances and profile requirements. We note that Ofcom does not have issue with the "all reasonable endeavours" requirement.

Q 8: Do you agree that it is appropriate to prohibit non-Zonal subnational pricing plans at this time? If not please state your reasons.

2.24 A subnational pricing plan is not of interest to Secured Mail, which operates on a fully national basis. In our view, it should be possible for access customers to operate effectively on the zonal access plan if the national plan is not suitable for their needs and we do not disagree with Ofcom's approach on this.

Q 9: Do you agree that the appropriate measure of cost in relation to our proposals is Zonal FAC by format? If not please state your reasons.

2.25 Secured Mail supports the use of LRIC rather than FAC for zonal costing (see 2.20)

Q 10: Do you agree with our proposal to use historic cost data rather than forecast data? If not please state your reasons.

2.26 Secured Mail believes Ofcom should use forecast costs, rather than actual costs, because forecast costs should (if Royal Mail is achieving efficiency improvement as Ofcom intends) be lower than past, actual costs and access users should be able to benefit as early as possible from efficiency improvement.

Q 11: Do you agree that we should require Royal Mail to use the 2012/13 ZCM, subject to a power for Ofcom to specify by direction that a different model be used? If not please give your reasons.

2.27 If Ofcom uses historic costs, Secured Mail does not disagree with what Ofcom proposes.

Q 12: Do you have a view on the appropriate volumes to use as weights in the weighted average rule? Please provide reasons for your view.

2.28 Secured Mail agrees with Ofcom that Royal Mail will not lose volume to E2E competition in an even way geographically or across Zones, and so there is likely to be increasing difference between RM's volume profile by zone and the true profile of mail. We therefore support Option 2, as including Royal Mail's USO volumes will lessen the distortion of Royal Mail's profile.

Q 13: Do you agree that it is appropriate to use format level volumes as the weights in the 'weighted average rule'? If not please give your reasons.

2.29 Secured Mail does not disagree.

Q 14: Do you agree with our proposal that the legal instrument implementing our proposed regulatory changes will come into force six months after the publication of the final Statement on this review? If not please give your reasons.

2.30 Secured Mail does disagree with Ofcom's proposal, but would welcome clarification from Ofcom on how the new obligations would apply to Royal Mail's January 2016 access prices (which must be announced in October 2015).

Q 15: Do you agree with the proposed scope of our review of the Zonal costing methodology to take place following the publication of our Statement? Are there any other issues that it would be appropriate to consider as part of the review?

2.31 Secured Mail does not disagree.

Q 16: Do you consider that there is a need for a structured compliance process with respect to the proposed remedies? If so, why and what would be the value of such a process, if not why not?

Q 17: If we were to establish a compliance process what form should it take?

2.32 Secured Mail believe information on compliance should be published, so that access users can be confident that Royal Mail's access prices are correctly set under the proposed requirements. We believe that means publishing the zonal cost ratios and volumes as a minimum.

Q 18: Do you consider there are reasons we should extend the access obligation to the crown dependencies? If so please state your reasons.

2.33 Secured Mail would strongly object to the removal of the crown dependencies from RM's access service.

2.34 Although there is little access mail volume for those destinations, they are of great importance to many access users and access would not meet their needs if the crown dependencies were excluded.

2.35 It is important that Royal Mail access services have the same geographic coverage as Royal Mail's retail services, which do include the crown dependencies, to avoid unfair discrimination between retail and access customers.

Q 19: Do you agree that our proposals are likely to address the concerns we have identified? Are there ways that Royal Mail could take action which would undermine the effectiveness of our proposals?

2.36 Secured Mail does not disagree that Ofcom's proposals are likely to address the concerns identified, but we have said above that we do not believe the proposals are enough to address the concerns fully, as they are unlikely to deliver benefit for all access users or be effective enough in driving Royal Mail to become fully efficient in a reasonable period.

Q 20: Do you agree with our assessment of the impact of our proposals? If not, please explain why.

Q 21: Do you agree with our proposals, if not please explain why?

2.37 Secured Notes that Ofcom expects the proposals will be good for Royal Mail retail customers and for E2E competitors, but bad for access operators – of which Secured is one.

2.38 If so, the proposals would seem to favour some competitors over others and could then distort the market.

2.39 We believe Ofcom needs to consider a general access price control or efficiency targets, to achieve balanced improvement for all mail users.

Q 22: does the way in which we have drafted the proposed modified access condition appropriately reflect the proposals and in particular do you find it sufficiently clear? In your response, you should suggest alternative wording if you have drafting concerns

2.40 Secured Mail believes the drafting reflects the proposals made and is clear.

Q 23: Which of our proposed two alternative definitions of ‘Relevant Postal Services’ discussed above do you prefer and what are your reasons for your preference?

Q 24: Do you agree with our proposal to base the concepts related to the concept and definition of ‘Zones’ on Royal Mail’s own methodology (as referred to above)? If not, please explain in detail why.

Q 25: Do you have any comments on our proposed new concepts and their definitions discussed in this Annex?

Q 26: Do you have any comments on our proposed corrections to the USPA Condition discussed in this Annex that are unrelated to our proposed new remedies in USPA 2.1A, USPA 6A and USPA 6B (and their associated new expressions)?

Q 27: Do you agree with our thinking and proposals for the rounding (decimal places) to assess compliance with our proposed new remedies in USPA 6A and USPA 6B? If not, please explain in detail why.

2.41 On Q23, please see our response to Q12

2.42 On the other questions, we do not feel we have the expert knowledge to comment.