

Jersey Competition Regulatory Authority



Initial Notice of the Proposed Grant of a Class I Postal Operator's Licence to High Speed Freight Services Limited

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Jersey Competition Regulatory Authority
2nd Floor Salisbury House, 1/9 Union Street, St Helier, Jersey , JE2 3RF
Tel 01534 514990, Fax 01534 514991 Web: www.cicra.je

JERSEY COMPETITION REGULATORY AUTHORITY

INITIAL NOTICE OF THE PROPOSED GRANT OF A CLASS I POSTAL OPERATOR'S LICENCE TO HI SPEED FREIGHT SERVICES LIMITED

Under Article 24 of the Postal Services (Jersey) Law 2004

The Jersey Competition Regulatory Authority ('JCRA'), in exercise of its powers under Article 15 of the Postal Services (Jersey) Law 2004 ('the Law'), proposes to grant to Hi-Speed Freight Services Limited ('HSFS') a Class I Postal Operator's licence ('Licence'). This document constitutes the Initial Notice of the proposed grant of the Licence, in accordance with Article 24 of the Law.

A copy of the proposed Licence is attached as Annex 1 to this Initial Notice.

Capitalised terms that are not otherwise defined in this Initial Notice take the meanings given to those terms in the proposed Licence.

The Licence would permit the conveyance of Packets and Large Letters from Jersey to addresses in mainland European destinations only¹, subject to a Minimum Volume Requirement. The conveyance of Letter format mail is excluded from the scope of the proposed Licence.

The Law requires the JCRA to perform its functions in a manner consistent with the duties set forth in Articles 8(1) and 8(2) of the Law. The JCRA's consideration of these duties in connection with its proposal to issue the Licence is detailed below.

Background

In 30 November 2010, HSFS submitted an application to the JCRA for a Class I Postal Operator's licence. HSFS's principal intention was to offer certain postal services (conveyance of Packets and Large Letters) to Jersey-based fulfilment companies.

On 19 October 2010, the JCRA published a Final Notice confirming its decision to award Class I Postal Operator licences to both Citipost DSA Ltd ('Citipost') and Hub Europe Ltd ('Hub'). Those licences permit the conveyance of Packets (with effect from 18 November 2010) and Large Letters (with effect from 1 January 2012).

On 24 November 2010, the JCRA published an Initial Notice advising of its proposal to grant a Class 1 Postal Operators licence to HSFS. A separate Initial Notice was simultaneously issued in relation to the JCRA's proposal to grant an identical Class 1 Postal Operator's licence to TNT Post UK Limited ('TNT Post'). The scope of the proposed licences was the conveyance and delivery of both Packets

¹ Excluding addresses in the UK, Isle of Man and other Channel Islands

and Large Letters; however, the proposed licences imposed no limitation on the geographical destination to which the mail items could be delivered. Written representations and objections to both Initial Notices were received from Jersey Post Limited, the Communication Workers Union ('CWU') and Hub Europe Ltd.

In early 2011, the JCRA learned that the UK Government was considering implementing a reduction in the threshold for Low Value Consignment Relief ('LVCR'). On 23 March 2011, the UK Chancellor of the Exchequer announced as part of the 2011 Budget that the LVCR threshold would be reduced from £18.00 to £15.00, with effect from 1 November 2011.

In June 2011, following the UK Government's decision to reduce the LVCR threshold, the Minister for Economic Development ('Minister'), Senator Alan Maclean, directed the JCRA to undertake a comprehensive review of the postal sector in Jersey. The Minister was concerned that further reductions in the level of LVCR would lead to a decrease in the volume of bulk mail carried by Jersey Post Limited ('JP'), which, it was feared, could jeopardise JP's ability to provide a universal postal service to businesses and households in Jersey. The Minister was aware that the JCRA had received applications for postal licences from TNT Post and HSFS, and wished to encourage the JCRA to gather information about the current and future financial position of JP under a range of scenarios with respect to LVCR before issuing any further licences.

During the review, the UK Government announced on 9 December 2011 that LVCR would be removed entirely with respect to commercial imports from the Channel Islands, with effect from 1 April 2012.

The JCRA has now completed its postal sector review, and has delivered its report to the Minister. It is expected that the report will be published (with appropriate redactions of confidential information) in due course.

Many of the conclusions reached by the JCRA in the postal sector review are relevant to the proposal to grant the Licence. Importantly, we identified that according to JP's own projections in its 2012 budget, JP will remain profitable even if its bulk mail business disappears completely. JP had previously calculated that the Universal Service Obligation ('USO') cost approximately £5 million per year to provide, and that its provision was only possible because of cross-subsidy from its bulk mail business. However, on the basis of JP's most recent projections for postage prices, cost savings and mail volumes, the JCRA has concluded that the provision of the USO generates sufficient profits for JP to fund it without the need of a cross-subsidy.

Consideration of HSFS's application in the light of the JCRA's duties under the Law

I. Considerations under Article 8(1) of the Law

1. The JCRA has a primary duty under Article 8(1)(a) of the Law to perform its functions “in such manner as is best calculated to ensure that (so far as in its view is reasonably practicable) postal services are provided, both within Jersey and between Jersey and the rest of the world, as satisfy all current and prospective demands for them, wherever arising”. In considering whether postal services satisfy demands under Article 8(1)(a), under Article 8(3), the JCRA must have regard, *inter alia*, to whether the services are rapid, of high quality and reliable, and are affordable by and accessible to, the highest number of business and domestic users.
2. The evidence suggests that there is demand, both current and prospective, for the postal services which would be provided under the proposed Licence. At present, JP’s bulk mail destined for addresses in continental Europe is routed through the UK, and carried by Royal Mail from the UK to other parts of Europe. Owing to this convoluted route, delivery times from Jersey to continental Europe are in the range of 5-7 days, which renders Jersey’s fulfilment industry less competitive in serving these markets.
3. As part of the postal sector review, the JCRA conducted a survey of bulk mail customers, and has also engaged in discussions with the 10 largest bulk mail customers. A clear majority of bulk mail users indicated that a bulk mail service to Europe that was able to reach destinations in 2-3 days would be of real benefit to their businesses. A number of those users projected significant increases in volumes if they were given access to such a service. These results indicate to us that there is current and prospective demand for such a service.
4. By contrast, bulk mail customers indicated general satisfaction with bulk mail services to the UK, Isle of Man and other Channel Islands. The JCRA is satisfied that the existing bulk mail services to those destinations meet the likely demand, and there is no indication that the service to be offered by the licence applicants for deliveries to those destinations would be materially different from the services currently on offer from Citipost, Hub and JP. Moreover, due to the removal of LVCR for commercial imports to the UK from the Channel Islands, future demand for such services is likely to be dramatically reduced.
5. In its application, HSFS proposes that it will use the spare capacity on an existing DHL aircraft service, which is currently used to convey DHL’s express mail in and out of the Island. If awarded a licence to convey bulk mail, HSFS contends that it would deliver Jersey-origin mail to DHL’s Leipzig hub in Germany by 9am the following morning. By being able to inject mail into European postal networks 1 day after posting, HSFS claims that it will be able to beat competitors’ services into Europe by at least 4-5 days. In addition, HSFS/DHL says that each mail item will be able to be fully tracked and traced.
6. Article 8(1)(b) of the Law also requires the JCRA to consider the effect, if any, that the grant of a Licence to HSFS may have on the financial resources available to JP. In the current context, the JCRA interprets this duty as requiring a consideration of the effect of its proposed decision upon JP’s ability to provide the USO in Jersey.
7. The JCRA is satisfied that the proposed grant of a Licence to HSFS will not jeopardise the ability of JP to finance the provision of the USO. It has reached this conclusion based on the following evidence:
 - As noted above, a key focus of the postal sector review was the sustainability of the USO. After a detailed examination of JP’s 2012 budget and its forecasts for 2013-

2014, the JCRA has concluded that, based on JP's most recent projections for postage prices, cost savings and mail volumes, the provision of the USO actually generates sufficient profits for JP without the need for cross-subsidy. On JP's own figures, provision of the USO does not rely on a cross-subsidy from its bulk mail business; indeed, JP has projected that even without its bulk mail business, it would still generate sufficient funds during 2012-2014 to sustain the USO.

- JP intends to pay a special dividend to its shareholder, the States of Jersey, in 2012, from its existing cash balances. Even after payment of this special dividend, JP's holding company will have significant cash reserves which could be used in part to fund the USO.
 - The proposed Licence expressly limits the format and the geographic destination of the mail items that HSFS can carry, as well as the customers that are entitled to use HSFS's service, as follows:
 - a) the proposed Licence is limited to the conveyance of Large Letters and Packets only, and not the conveyance of Letter format mail;
 - b) the proposed Licence only permits the conveyance of mail to addresses in mainland Europe, so that the bulk mail business of JP serving the UK, Isle of Man and other Channel Islands will be unaffected; and
 - c) the proposed Licence has a Minimum Volume Requirement, under which HSFS can only convey mailings of 50 or more items for Large Letters, and/or mailings of 25 or more items for Packets.
 - The JCRA retains discretion under the proposed Licence (and the licences already issued to Citipost and Hub) to introduce a USO funding mechanism should JP be able to show that the provision of the USO represents an unfair burden on JP².
8. With respect to the considerations set out in Article 8(3), as noted above, the JCRA expects that the services provided under the proposed Licence will be more rapid than those currently available to postal users in Jersey. In its application, HSFS claims that the proposed services will be rapid (comparable to any other provider), and that it has a track record of high quality and reliability. Furthermore, the services to be offered will be competitively priced and accessible to users sending Large Letters or Packets, subject to the Minimum Volume Requirement, as well as being tailored to meet potential users' requirements. Finally, customers of HSFS will have the opportunity to express views on the service provision. The JCRA has no reason to doubt any of these statements.
9. The JCRA therefore believes that the proposed grant of the Licence to HSFS is consistent with its duty under Article 8(1)(a) of the Law.

II. Considerations under Article 8(2) of the Law

² See Article 17(1)(h) of the Law and Condition 19 of the proposed Licence.

10. Article 8(2) of the Law specifies certain additional duties to which the JCRA must have regard, although only in so far as is consistent with its primary duty under Article 8(1). The JCRA's consideration of these Article 8(2) duties is set out below.

A. Article 8(2)(a)

11. The JCRA has a duty under Article 8(2)(a) to perform its functions "in such manner as it considers is best calculated to protect and further the short- and long-term interests of users within Jersey of postal services, and to perform them, wherever it considers appropriate, by promoting competition among persons engaged in commercial activities connected with postal services in Jersey".
12. The benefits of competition, in terms of the benefits which it brings to users in the way of lower prices, greater choice and innovative products and services, are well known. In the postal sector, the 2008 Hooper Report³ and the 2010 updated Hooper Report⁴ looked at policies which may be needed to ensure the continued provision of the universal service. As regards competition, the 2008 Report concluded that competition between postal operators can support the universal service by encouraging cost reductions by the universal service provider, and therefore greater efficiency. Furthermore, such competition should encourage innovation in the products and services offered, which can create further revenue streams to support the universal service (see, in particular, page 95 of the Report).
13. The Hooper Report did recognise that in the UK since 2005, large businesses have benefited from liberalisation through lower prices and that these benefits might not otherwise have been expected without competition. The Report also stated that while competition is beneficial to consumers, it does also entail some risks, such as a potential reduction in the revenue stream available to support the universal service. It also stated that some forms of competition can be inefficient if they take advantage of constraints which might be placed upon the universal service provider. On balance, however, the Report concluded that these risks were manageable.
14. In the EU countries where postal markets have been liberalised (e.g. The Netherlands, Germany and the UK), competition has prompted significant increases in efficiency by the incumbent. Indeed, evidence collected from bulk mail customers during the postal by granting the proposed Licence, the JCRA believes that it will create more customer choice and ensure that postal services for these items are as customer-responsive, cost-effective and efficient as possible.
15. As noted at paragraph 6 above, the JCRA has considered the potential risks of this decision to JP's provision of the USO, but for the reasons set out there, does not consider that the grant of the proposed Licence to HSFS would prevent JP from continuing to provide the USO. For those reasons, the JCRA believes the grant of the Licence is consistent with its duty under Article 8(2)(a).

B. Article 8(2)(b)

³ Hooper (2008), *Modernise or decline: Policies to maintain the universal postal service in the United Kingdom*.

⁴ Hooper (2010), *Saving the Royal Mail's universal Postal Services in the digital age – An update of the 2008 Independent Review of the Postal Services Sector*

16. The JCRA has a duty under Article 8(2)(b) to perform its functions “in such manner as it considers is best calculated to promote efficiency, economy and effectiveness in commercial activities connected with postal service in Jersey”. It is widely recognised that the introduction of competition serves to increase productive, dynamic and allocative efficiency. Currently JP, Citipost and Hub are the only providers of bulk mail services to the fulfilment industry in Jersey, and only JP presently offers bulk mail services into Europe. The JCRA is satisfied that the proposed grant of the Licence would facilitate the promotion of competition for postal services and thereby advance the Article 8(2)(b) objectives.

C. Article 8(2)(c)

17. The JCRA has a duty under Article 8(2)(c) to perform its functions “in such manner as it considers is best calculated to further Jersey’s economic interests”.
18. The JCRA is still of the view it expressed in the April 2009 consultation regarding the proposed grant of a Licence to Citipost and Hub⁵ as to the likely benefits to Jersey’s fulfilment industry of new licences to provide bulk mail services:

“Should the grant of a licence to Citipost and Hub result, through competition, in lower prices for postal services to existing providers of fulfilment services, this could potentially enable them to cut their costs and become more competitive against fulfilment companies located in other jurisdictions. More diverse postal fulfilment services may also attract new providers of fulfilment services to Jersey. Finally, greater competition in the provision of postal services to fulfilment companies may also benefit Jersey by giving incentives to current providers of fulfilment services in Jersey to stay located in this jurisdiction. The JCRA has observed in the past that while JP currently holds a monopoly for the provision of fulfilment services in Jersey, Jersey itself faces competition from other offshore jurisdictions (such as Guernsey and Switzerland) as a platform from which to provide such services⁶.”

19. The potential benefits of the grant of the proposed Licence are brought into starker focus by the decision of the UK Government to remove LVCR for commercial imports from the Channel Islands with effect from 1 April 2012. Based on the JCRA’s discussions with bulk mailers conducted as part of the postal sector review, it appears very likely that the removal of LVCR will vastly reduce bulk mail exports from Jersey to the UK. The reduction in size or outright closure of fulfilment firms is likely to have a major impact on both economic activity and employment levels in Jersey, given the importance of the industry at present, and the current elevated levels of unemployment.
20. However, the decision of the UK Government has no effect on the ability of Jersey-based fulfilment businesses to export goods to other countries within Europe. As noted above, the JCRA’s survey of bulk mailers indicated that these customers want quicker bulk mail services from Jersey to continental Europe, and expect that their exports to Europe could

⁵ JCRA consultation on Citipost DSA Ltd’s application for a Class I Postal Operator’s Licence, 8 April 2009.

⁶ JCRA Final Notice to Jersey Post Limited Concerning Price Control, 22 November 2007.

increase considerably if such a service were available. The JCRA understands that many fulfilment businesses are currently considering the future of their businesses in Jersey, given that removal of LVCR for exports to the UK will take place in less than 4 months. The JCRA's expectation is that improved bulk mail services to Europe would result from the proposed grant of the Licence. To the extent that such services encourage fulfilment businesses to retain some activities in Jersey so as to serve European markets, then the JCRA is satisfied that the grant of the Licence would further the economic interests of Jersey.

D. Article 8(2)(d)

21. The JCRA has a duty under Article 8(2)(d) to perform its functions "as it considers is best calculated to impose a minimum of restrictions on persons engaged in commercial activities connected with postal services in Jersey".
22. The proposed Licence does impose restrictions on the format (ie Packets and Large Letters only) and the geographic destination (i.e. mainland Europe only) of the mail items that HSFS can carry, as well as the customers that are entitled to use HSFS's service (through the imposition of the Minimum Volume Requirement). The JCRA has included these restrictions in the proposed Licence in order to limit the effect of the grant of the Licence on the ability of JP to provide the USO, and to ensure that the activities of HSFS are directed to the identified area of unmet current and prospective demand. The JCRA is satisfied that these restrictions are the minimum necessary in order to ensure that the JCRA's primary duty in Article 8(1) of the Law is satisfied in connection with the proposed decision to grant the Licence.

E. Article 8(2)(e)

22. The JCRA has a duty under Article 8(2)(e) to have regard to the need to ensure that postal providers have sufficient financial and other resources to conduct postal activities.
23. Hi-Speed has already been awarded with a Class 1 Postal Operator's Licence to convey Licensed Letters from Business customers located in Jersey for collection by DHL Global Mail (UK) Ltd, for onward conveyance and final delivery to International destinations.
24. Hi-Speed is the Jersey agent for DHL, one of the market leaders in providing express mail solutions both within Jersey and between Jersey and the rest of the world. In Jersey, Hi-Speed employs 29 people and has over 160 corporate customers. The JCRA has been provided with sufficient evidence from its 2009 accounts to satisfy itself that Hi-Speed has sufficient financial and other resources to conduct the activities to be covered by the Licence.
25. Similarly, for the reasons given in paragraphs 6-8 above, the JCRA believes that the grant of the Licence will not jeopardise the financial ability of JP to satisfy its current USO obligations.

F. Article 8(2)(f)

26. Article 8(2)(f) requires the JCRA to have regard to "any special needs of persons

who are disabled or have limited financial resources or other special needs”. The JCRA believes that the grant of the Licence will be neutral in terms of its effect on the categories of persons identified in Article 8(2)(f).

III. Date when the proposed Licence will take effect

27. The proposed Licence will take effect on **24 February 2012**, unless the JCRA receives representations or objections about the proposal prior to that date, in which case the effective date will be specified in any Final Notice issued by the JCRA under Article 24(5) of the Law.
28. A copy of the draft Licence is available for inspection between the hours of 09-00 and 17-00 Monday to Friday at the offices of the JCRA (address set out below). A copy is also available on the JCRA’s website, www.cicra.je.

IV. Period for written representations or objections

29. Any written representations or objections in respect of the proposal to grant this Licence may be made by midnight on 23 February 2012 to the JCRA at:

Jersey Competition Regulatory Authority
2nd Floor, Salisbury House,
1-9 Union Street,
St. Helier, Jersey
JE2 3RF

or by e-mail to paul.hamilton@cicra.je or by fax to + 44 (0) 1534 514991

9 January 2012

By Order of the Board of the JCRA