

GOVERNMENT REVIEW OF THE BALANCE OF COMPETENCES BETWEEN THE UNITED KINGDOM AND THE EUROPEAN UNION

Royal Mail response to the call for evidence: Competition and Consumer Policy Review

Royal Mail welcomes the opportunity to provide the Government with a brief overview of the EU and UK competition rules that apply in the postal sector and to set out what it believes to be the biggest challenges facing regulators and policy makers at both the EU and UK level: the sustainability of the Universal Postal Service.

The first part of this paper provides an introduction to Royal Mail and the EU and UK competition and regulatory framework in which it operates. In the second part, Royal Mail sets out the action it believes is required at the UK and EU levels to protect the Universal Postal Service. Royal Mail would welcome the opportunity to discuss the points raised with all interested stakeholders within Government.

Part 1: Background to Royal Mail and the application of competition law in the UK postal sector

The UK's postal sector is, like any other in the EU, subject to the general EU and UK competition law prohibitions against anti-competitive agreements (Article 101 TFEU / Chapter 1 of the Competition Act 1998) and abuse of a dominant position (Article 102 TFEU / Chapter 2 of the Competition Act 1998).

While there are differences between the UK and the EU competition regimes (for example, the existence of a criminal cartel offence in the UK), the rules are substantively the same. Royal Mail follows developments in both regimes with equal interest. In general, Royal Mail believes that the UK and EU competition rules, as well as the EU's rules on state aid, are (while not without their uncertainties and weaknesses) relatively well-established and well-understood in the UK and beyond.

Royal Mail must also comply with a range of sectoral regulatory obligations that supplement the general competition rules. For example, Royal Mail is required to allow, in certain circumstances, other postal operators access to its network and is subject to a range of related obligations including a regulatory margin squeeze test on its pricing. These regulatory rules are UK specific, although they are consistent with EU law. For instance, the general principle of allowing access to postal infrastructure is recognised as a possibility in the EU's postal legislation (principally, Directive 97/67/EC as amended) and provisions analogous to those in the UK can be found in other EU Member States.

The general competition and sector specific regulatory rules have to be viewed in conjunction with the recognition at both the EU and UK levels that the provision of postal services is an essential instrument of communication, trade and social and territorial cohesion. Market liberalisation, achieved in the UK in 2006 and required of all Member States under EU rules as at 1 January 2013, has therefore proceeded hand in hand with a stated policy and legal objective of safeguarding the provision of a Universal Postal Service: that is, a user's ability to benefit from a postal service of a specified quality at an affordable price across the national territory.

Safeguarding the Universal Postal Service is a fundamental aspect of both the EU's postal legislation and the UK's principal legislation in the postal sector, the Postal Services Act 2011: the latter specifically provides that the primary duty of Ofcom (the UK's postal regulator) is to secure the provision of (a financially sustainable and efficient) Universal Postal Service.

This is the wider context in which the application of EU and UK competition law and the appropriateness / workability of any supplemental regulatory obligations should be understood and applied in the postal sector.

Royal Mail: Working to deliver the Universal Postal Service

Royal Mail is the designated provider of the UK's Universal Postal Service. This means that, under UK law (Postal Services Act 2011), Royal Mail is obliged to collect and deliver letters six days a week (and parcels five days a week) at an affordable and geographically uniform price to every address in the UK. The six days a week required service for letters goes beyond the five days minimum required under the EU's postal legislation. Another requirement under UK law that goes beyond the EU's postal legislation is that Royal Mail must provide postal services at not just an affordable price (a feature of the EU's postal legislation), but also at a uniform price (not a specific requirement under the EU's postal legislation). Indeed the UK has often acted well in advance of what is required under EU law. For instance, the possibility of mandated access has existed in the UK since 2001 (under the terms of Royal Mail's then licence) whereas at the EU level it was not until December 2010 that the EU's postal legislation required (subject to certain conditions) access to be provided to elements of the postal infrastructure or services provided within the scope of the Universal Postal Service.

The provision of the Universal Postal Service is an obligation that Royal Mail is proud to discharge. Through the Universal Postal Service, Royal Mail ensures that, wherever an individual or business is based, they are not excluded from the postal service system. The Universal Postal Service delivers essential economic and social welfare benefits to individuals and businesses across the UK.

The Universal Postal Service has a strong social and economic value. Individuals and businesses can post mail overnight from, for example, Edinburgh to Exeter or Belfast to Birmingham, at a uniform price that compares favourably with many everyday items in terms of affordability, value for money and quality of the product provided. The Universal Postal Service as delivered by Royal Mail meets the reasonable needs of postal users and is highly valued by residential and business users, as Ofcom recognised in its March 2013 Review of Postal Users' Needs.

The obligation on Royal Mail to provide the UK's Universal Postal Service requires Royal Mail to maintain an inherently high cost network infrastructure. Royal Mail must be capable of delivering to 29 million addresses, and collecting mail from around 115,000 post boxes, 11,800 Post Offices and 80,000 businesses at least once a day. Royal Mail helps small and large businesses find new customers as well as delivering to their existing ones, enabling commerce to thrive through our deep postal delivery network. Other postal operators can benefit from this network through the regulatory requirement on Royal Mail to allow them access to its delivery services (mandated access).

The £7.1 billion annual costs of the Universal Postal Service network can only be covered if the costs of delivery to unprofitable, low density rural areas are supported by profits from more profitable high density urban segments of the network. The structural decline in the letters market makes it increasingly challenging to ensure the financial sustainability of the Universal Postal Service.

Part 2: Managing the threat to the Universal Postal Service

Both the EU and the UK have sought to open up the postal sector to competition. Royal Mail embraces fair competition, but believes that competition that delivers positive outcomes for individuals and businesses throughout the UK and across the EU can only be achieved if there is a level playing field.

Ofcom's primary duty is to secure the provision of (a financially sustainable and efficient) Universal Service. The financial viability of the Universal Postal Service is jeopardised if competitors can cherry-

pick profitable urban markets in which to provide end-to-end services, while simultaneously (through the mandated access system) requiring the Universal Postal Service provider to complete the delivery of less profitable mail.

This is currently the threat faced in the UK, where other postal operators are in a position to undercut Royal Mail on price as they do not bear the costs of the Universal Postal Service while still retaining the ability to use Royal Mail's network (through the mandated access system) where that is to their commercial benefit. This situation is already gathering pace in the UK. This would further threaten the current postal service, especially in relation to deliveries to and from remote parts of the country. Those who live, work and run businesses in these areas, will lose out.

Providers of the Universal Postal Service need to make a reasonable commercial rate of return on the provision of the Universal Postal Service for it to be sustainable. The need for a financially sustainable Universal Postal Service is specifically recognised in the Postal Services Act 2011. It is an issue to which Ofcom must have regard in carrying out its primary duty of securing the provision of the Universal Postal Service and it must remain the key objective for the UK Government, the EU and its Member States, now and in the future.

Allowing unfair competition, in the form of unfair cherry-picking, will undermine the viability of the Universal Postal Service, to the long-term detriment of individuals and businesses across the UK and Europe.

We believe that the European Commission, and the European Regulators Group for Postal Services (a body established by the European Commission in 2010 and comprised of the Member State's postal regulators), may have underestimated the speed at which direct delivery competition could become a risk to the financial sustainability of the UK's Universal Postal Service.

Royal Mail believes that the UK Government must clearly and consistently highlight this threat to the Universal Postal Service in its EU interactions, including through proactive involvement in the European Commission's ongoing review of the EU's postal legislation. The UK Government must work with its EU partners and other stakeholders to achieve an effective solution that marries effective competition with a sustainable Universal Postal Service.

This EU action needs to be supplemented by action at the national level which needs to be set in motion now. In particular, it is essential for Ofcom to bring forward its planned 2015 review of direct delivery competition. Work needs to start now at the UK level, where the particular combination of a mature access market, strong e-substitution and direct delivery mean that the threat to the Universal Postal Service is acute.

The UK, as does the EU, needs a clear and effective regulatory framework for postal competition on fair terms that prevents cherry-picking, and, critically, maintains the financial sustainability of the Universal Postal Service that reaches all citizens and businesses at an affordable price, and supports business growth.

Royal Mail believes the UK must ensure that the EU strikes a proper balance between fair competition and the sustainability of the Universal Postal Service. The UK postal sector has reached a critical stage that needs proactive management and, including through action at the national level, the UK Government has the opportunity to shape the EU agenda and lead the EU's actions in this area.

We would be happy to meet with you and elaborate further on the written points we make above.

