



Comments on 2006 Postal Pricing Review: Process and Timetable – Consultation Paper

Guernsey Post Response

October 2004

1.0 Introduction

The Office of Utility Regulation (OUR) published on 10th September its consultation document designed to explain the process and timetable that it intends to follow in carrying out its review of Guernsey Post's pricing proposals for 1st April 2006.

Whilst Guernsey Post was aware of the broad timetable and had already commenced work on those areas due for submission to the OUR on 1st November, it was not aware that a public consultation was to be launched on the process simultaneously with the publication by Treasury and Resources of Guernsey Post's year end accounts for 2002/03 and the Company's own consultation on the future of the retail network, both of which had been discussed with and signalled well in advance to the OUR.

Earlier reciprocal notification by the OUR to Guernsey Post of the consultation on the pricing review process would have facilitated better resource planning, as considerable additional workload has fallen to key staff who are inevitably involved in both the OUR and Guernsey Post consultations. In this regard, it must be remembered that whilst processes modelled on those operated by Postcomm, the UK regulator, are sound, they are managed by Royal Mail through a substantial regulatory department, unlike the situation in Guernsey where only a few managers are able to respond to OUR requirements and they already have a day-job.

Notwithstanding this, Guernsey Post believes that given the unavoidable and substantial costs likely to impact its bottom line from April 2006, after the re-negotiation of the Royal Mail contract, a tariff increase with effect from 1st April 2006 will be essential. Furthermore, there are clear learning points from the tariff determination process undertaken in 2003/04 from which all parties could learn, not least the adoption of certain project management techniques, where pragmatic, though robust specification, of the deliverables would greatly enhance the process. The Company therefore welcomes the invitation to make a submission to the OUR in this regard.

The remainder of this response is organised as follows:

- Section 2: reviews the OUR's postal work programme
- Section 3: reviews Royal Mail's activities
- Section 4: reviews the 2003/04 process
- Section 5: looks at the work already scheduled by Guernsey Post to continue the successful change process from Government department to commercialised States-owned utility.
- Section 6: reviews the suggested timetable
- Section 7: summarises the Guernsey Post views on the 2006 tariff determination process

2.0 OUR's Postal Work Programme

2.1 Price regulation of non-licensed services

Guernsey Post considers this parallel piece of work to be very significant for the company as a whole. Again, however, it was launched as a consultation at the same time as the present process review and with less than 24 hours prior notice. Guernsey Post asked for an additional month to take legal advice etc and is disappointed that the Director general has felt constrained to disallow this. The Company regards the clarity of definitions needed to support this extension of her powers warrants more work up front in the best interests of Guernsey Post and its customers and other stakeholders, and in particular in determining the extra work and resource needed during the impending pricing review process.

2.2 Size of the reserved sector

On 18th February 2004 Guernsey Post submitted a paper on the assessment of the cost and revenue generated by the Universal Service Obligation (USO) and the reserved services respectively. The OUR did not take this into account within the 2004 tariff determination and indicated that any consideration of the reserved sector would require a public consultation to allow interested parties to comment.

In order to consider the Guernsey Post proposals regarding the cost and revenue of the reserved sector, the OUR considered it necessary for Guernsey Post to consider the appropriate service specification for the USO within the Bailiwick.

As indicated, the initial requirement for this review was borne from Guernsey Post's need to secure adequate revenue to fund the USO when the bulk sector was operating outside the reserved sector. The determination of 1st March 2004 negated this immediate need but with the Bulk Mailer Association lobbying for a "cost +" pricing regime from 2006, this work to determine the saving available from changes to the USO and quality drivers against which the company operates remains important.

A project to review these matters has been underway for some time and consultation with interested parties has begun; however completion on time, 1st November 2004, could be jeopardised, given current difficulties in agreeing dates for consultation with certain of the interested parties, and the need to take their views on board before the due completion date. Guernsey Post may separately need to request an extension in the timescale.

2.3 Compliance with quality of service targets

Guernsey Post has been submitting its improving quality of service figures to the Director General more frequently than required within the terms of its Licence. Therefore at all times the OUR has been kept informed of progress or otherwise in this area. The reports that are required to review the six-month period April – September for operations and customer service will be submitted together with the annual return for the previous 12 months, by 31st October 2004 as specified within the Licence.

2.4 Postal monitoring and development plan

The first submission of this document is also scheduled for 1st November 2004. A comprehensive document reviewing the processes used across the company to monitor actual performance; the process for the collection and analysis of suitable data; and the procedures for internal review and performance improvement planning by Guernsey Post must be produced in accordance with the Licence. Beyond the above, the exact nature of the requirement has not been clearly defined and its development is indeed to be an iterative process: Guernsey Post hopes that the existing quality of service reporting will suffice if coupled with the reports to the Company's strategic programme board which oversees and manages the implementation through project management of change projects and strategy across its five business units and the supporting functions.

3.0 Royal Mail's activities

3.1 Postcomm's consultation on early liberalisation of the UK postal market

After the publication of the OUR consultation paper, on 20th September 2004 Postcomm announced its consultation on a package of measures designed to bring forward competition in postal services, promote greater efficiency and service quality from Royal Mail and make it easier for competitors to enter the market. The proposals would advance Postcomm's current timetable for full market opening by 15 months to 1st January 2006, provide Royal Mail with an extra nine months to prepare for full liberalisation by cancelling the interim stage of market opening that had been planned for April 2005, safeguard the continuing provision of the universal service for 1st and 2nd class stamped post at a geographically uniform price and set a framework for Royal Mail's price and service quality control from April 2006. The proposals will also provide more freedom to Royal Mail to offer new, innovative services to help it compete in the fully liberalised market and give customers more choices, so they can select a postal supplier that meets their service quality requirements and offers innovative postal products. This has been welcomed by Royal Mail subject to simple, light-touch regulation allowing the company to make an acceptable rate of return on its turnover. Guernsey Post agrees with the Director General that such changes could have a beneficial impact on the Company in the medium-term, but the extent of that impact is difficult at present to foresee.

3.2 Royal Mail pricing structure

Sized based pricing is unlikely to be introduced before April 2006, according to the UK postal regulator. Until now it was thought that the new pricing system could be introduced as early as September 2005, which may have impacted Guernsey Post within the life of the current price control period. However the consultation in the UK generated over 9,000 responses and Postcomm is undertaking a thorough analysis of all the feedback, while continuing to work with Royal Mail on understanding the cost justification for the proposals. How this new pricing regime, if agreed and introduced in April 2006, may impact the renewed contractual negotiations between Guernsey Post and Royal Mail remains to be seen. What is certain, is that until the UK market has stabilised after this traumatic period of change, there is substantial resource-hungry market development, risk assessment and financial modelling work to be undertaken by Guernsey Post to ensure it achieves the best deal possible in the short term without severing options that may develop in the medium to longer term.

It should be noted that by the very nature of these developments, Guernsey Post is not privy to either Royal Mail's or Postcomm's deliberations. Furthermore the OUR pricing review process, Guernsey Post's contractual negotiations with Royal Mail, and Royal Mail's discussions with Postcomm are happening in parallel, making the whole process highly complex and the last two

may not fit into the timescale of the first. Guernsey Post is, however, endeavouring to obtain the agreement of Jersey Post, Isle of Man Post (who are both part of the Tri-Island negotiating team) and Royal Mail to accomplish the contractual negotiations for April 2006 within the OUR's proposed timescale.

However, Guernsey Post would not wish this timescale to put undue pressure on the negotiating team that might lead to a sub optimal outcome.

4.0 OUR Postal Price Review Process

The OUR postal price review process which led to the document OUR 04/02 was inevitably also a learning process for both the OUR and Guernsey Post. It was the first time that either had been involved in the mechanics of regulatory postal price control and such inexperience manifested itself in an occasional lack of clarity which impaired either organizations' understanding of what the other was expecting of it; this at times, regrettably, impacted on customers, especially the bulk mailers.

For example, some tentative information, in what remains a highly competitive market, was provided by Guernsey Post at the start of the exercise on the potential drop in bulk-mail discounts: more in December 2003 at the request of the OUR in the face of continuing requests for such information from the bulk mailers; and finally the OUR proposed a completely different price regime for them, without consultation with Guernsey Post, and to a timescale that was contractually unacceptable to the bulk mailers.

Nor did Guernsey Post actually know what the price control period was going to be (i.e. 1st April 2004 to 31st March 2006) until document OUR 04/02 was published. Indeed, the contractual obligation with bulk mailers in effect foreshortened that period in terms of revenue benefit to Guernsey Post.

In addition repeated and sometimes duplicatory requests for information were made by the OUR in December 2003 and January 2004 which might have been alleviated if the requirements had been better defined at the outset, and OUR and Guernsey Post resources had been rescheduled. For example

- OUR Information Request C was issued 5th December 2003, which was the due date for the Guernsey Post response to Information Request A. Information Request B was work in progress at the time.
- There were questions raised in Information Request C that had already been covered in Requests A and B; C3 = B17, C4 = Annex to B, C6 = B21 and C14 = A2.

Reference	Information Request Issued	Response Due Date	Guernsey Post Response Date
A	21 st November 2003	5 th December 2003	3 rd December (draft) 9 th December final
B	1 st December 2003	12 th December 2003	11 th December 2003
C	5 th December 2003	19 th December 2003	19 th December 2003
D	29 th December 2003	9 th January 2004	16 th January 2004
E	20 th January 2004	21 st January 2004	22 nd January 2004
Meetings	4 th February 2004	5 th February	10 th February 2004

The frustration in Guernsey Post is the perception that the OUR is not prepared to define adequately what it requires in advance, but prefers to await the end product before defining that requirement. This is not good project management and inevitably, without defined specifications or quality criteria, leads to suboptimal deliverables and potentially to delay.

It is important, therefore, for both sides to take account of these learning points in proceeding with the second postal pricing review. There are already a number of references in document OUR 04/19 that will need careful specification in advance, both in terminology and intent, especially as the OUR seeks one year of historical data and a six year forecast in the Guernsey Post Business Plan. At what level of detail, what tolerances, what are the data sources in the absence of co-operation from bulk mailers, and will business planning data received by OUR be made available to Guernsey Post if decisions are based on it in preference to the Guernsey Post data? Guernsey Post notes that “the OUR intends to engage with Guernsey Post over coming months to ensure that the Company’s Business Plan will satisfy the OUR’s requirements and can be readily incorporated with the OUR’s own economic model.” The Company urges the OUR to consider adopting project management techniques and requests that the OUR provide more detailed definitions of its terms to address such issues as:

- “the requirement for **more robust** business planning for **longer term** price setting” (para 4)
- “if it is proposed to consider making a finding of dominance in a relevant market, an **appropriate consultation** will be undertaken (between November 2004 and February 2005) on any such proposals “ (para 4.1.3)
- the consultation on the size of the reserved sector “is likely to take place in the period November 2004 to February 2005, but this is dependent on the **quality and details** of Guernsey Post’s submission and any requirement to seek additional information could impact on the consultation”. It has proved difficult for Guernsey Post to obtain a clear understanding of the “quality” and “detail” required (para 4.1.4)

There is also the paradox inherent in para 4.2.2 that the OUR would welcome bulk mailers providing information on, inter alia, their demand for postal services; accepts that bulk mailers are not obliged, and may be unwilling, to provide it; but needs it to assess Guernsey Post’s volume forecasts. Whence is Guernsey Post expected to obtain this information, if bulk mailers are even unwilling to provide it in confidence to a third party? Should the OUR and Guernsey Post not agree an acceptable approach to such forecasting in advance?

In short, Guernsey Post believes that the process can be substantially improved by adherence to a degree of project management. While it is accepted that the OUR could not take part directly in Guernsey Post’s internal project aimed at producing its tariff submission, nevertheless, it could assist in providing clear product descriptions as defined in the PRINCE2 methodology used by Guernsey Post.

The OUR is therefore requested to assist the Company in adhering to Direction 1 of March 2003 (OUR 03/06A, para 5.3.3) which required it “to adopt an effective project-planning methodology for all projects carried out by the Company that affect its provision of Licensed Services”.

5.0 The timetable

Document OUR 04/19 provides some indication of the key consultation and information requirements that the OUR considers are crucial to the review of 2006 postal prices and sets out a proposed timetable for the work required to complete the review.

Guernsey Post agrees that the key driver in setting the timetable is the desire for any new prices to be publicly known well before the implementation date of 1st April 2006 so as to enable all parties to prepare and plan for those new prices.

Reviewing the process as set down in section 4.3 of the consultation document, Guernsey Post would comment that it has responded separately to the proposals to modify its Licence to enable the consideration of price control for non-licensed services in areas where the company is determined to be dominant and therefore will not comment further on either this consultation or that which may result as a consequence of it.

As regards the work that Guernsey Post has undertaken to satisfy the OUR needs to review the USO and supporting revenue from the reserved sector, comment has been made above that the submission may need to be made later than the current 1st November date because the consultation process with interested parties is proving challenging. This may impact on the time frame that OUR has indicated for consultation on these findings across a wider audience.

Guernsey Post has anticipated a submission date of 1st August 2005 for its tariff application given previous discussion with the OUR and notes that it is proposed within this timetable to push this back to September 2005. Given the comments below, Guernsey Post would recommend adherence to the original date of 1st August 2005, provided that clear and precise deliverables are established up front.

Guernsey Post would seek an earlier announcement date of the OUR's determination on its application. The lead-time necessary to seek Royal Approval for the new stamps, their production and distribution is substantial. Experience in 2004 indicated that the 12 weeks available was insufficient as customers required access to the lead rate stamps over the counter at least 2 weeks before the change in rates was operational. This reduced the stamp approval and production period to 10 weeks, where 14 weeks is the standard operational requirement for the Philatelic business model. Additionally there are contractual obligations between Guernsey Post and its key customers, the bulk mailers. In 2004 the OUR determination completely changed the tariff regime for these customers, and particularly the date for its introduction, without any prior indication to Guernsey Post. This unilateral step created contractual problems that cost Guernsey Post a little under £700,000 to resolve.

The OUR is therefore requested to assist the Company through the publication on 1st December 2005 of its determination on the postal prices with effect from 1st April 2006.

Guernsey Post would, in this circumstance, submit its tariff application to the OUR on 1st August 2005.

6.0 Summary

Guernsey Post welcomes the opportunity to respond to consultation document OUR 04/19 regarding the process to be adopted for the next postal price review and supports the view that the key driver in setting the timetable is the desire for any new prices to be publicly known well before the implementation date of 1st April 2006 so as to enable all parties to prepare and plan for those new prices.

Guernsey Post believes it has evidenced the need to agree the structure and breadth of the application in advance of work commencing in order to address the OUR concerns around the detail and quality of information. An iterative process, as in 2004, provided a learning opportunity for all interested parties but resources are precious and need to be deployed in a structured manner from the commencement of the project. Indeed this approach supports the OUR's own Direction issued to Guernsey Post in March 2003 regarding the adoption and use of project management techniques – and a task of the size and complexity of a tariff application undoubtedly needs an agreed project initiation document supported by detailed product specifications for the projects outputs specifying the acceptable tolerances on data accuracy, a supporting communications plan, a mid-point assessment and importantly, given the costs incurred by changes to tariff regimes, project assurance.

Guernsey Post recognises that some of these standard processes create conflict for a transparent regulatory regime but it is confident that a compromise balancing the needs of both key parties can be achieved within the framework of PRINCE 2 project methodology.

In closing, the Company would reiterate that it requires an announcement date of 1st December 2005 in order to de-risk the implementation process as far as is practicable given the environment in which it operates. It therefore recommends that it submits its application on 1st August 2005 as originally indicated by the OUR.

ends