



Office of Utility Regulation

Guernsey Post's Proposed Tariff Changes

Consultation Paper

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Office of Utility Regulation

Suites B1 & B2, Hirzel Court, St Peter Port, Guernsey, GY1 2NH
Tel: (0)1481 711120, Fax: (0)1481 711140, Web: www.regutil.gg

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1. Introduction

The Director General of Utility Regulation (“DG”) has received an application for tariff changes from Guernsey Post Limited (“GPL”). GPL has applied to revise its postal tariffs with effect from 1st April 2006. Full details of GPL’s proposed tariff changes are published on GPL’s website and also included as an annex to this document. The public document sets out the company’s proposed price changes and includes their rationale for the price increases they are seeking.

In OUR 04/23 the DG published decisions on the timetable and process for the review of GPL’s tariff application as the current price control on GPL will end on 31st March 2006. GPL submitted its tariff application and detailed Business Plan in mid August and the OUR is now conducting the public consultation described in OUR 04/23.

This consultation document includes a summary of GPL’s proposed tariff changes which has been received by this Office together with a description of the methodology the OUR intends to adopt in reviewing GPL’s tariff change submission. The OUR is therefore inviting comments from all interested parties on both:

- GPL’s proposed price changes; and
- the OUR’s methodology for assessing the reasonableness of the tariff changes sought by the company.

In parallel with this consultation interested parties should be aware that the OUR has recently published a notice of a proposed decision¹ of findings of dominance in Guernsey’s postal market. In that paper the DG has stated that, based on the information available to him on the postal market in Guernsey he proposes to find GPL dominant in the following markets:

- Regular postal services for letters and parcels up to 20kg;
- Priority postal letters and parcels markets; and
- Bulk mail services.

The deadline for responses to the statutory invitation to comment on the dominance findings is 30th September 2005.

In undertaking this consultation the DG is cognisant of the impact that the proposed tariff changes may have on all users of the postal service in Guernsey. He is also aware that for many businesses, particularly the bulk mail industry, the postal service is a significant input to their underlying business. He therefore is seeking, through this consultation, detailed responses from postal users of the possible impact that changes of the type being proposed by GPL may have on their use of the postal service.

The DG recognises that the commercial environment in which GPL currently operates has changed significantly since 2001. Its underlying cost base has incurred a significant step change as a result of the new charging arrangements with Royal Mail. As was identified in the previous price control decision in March 2004, the proposed price increases are driven to a large degree by external factors primarily with its major

¹ OUR 05/21

partner, Royal Mail and the changes within the UK regulatory regime. These changes are set out in more detail in Section 4 of this consultation document. In summary, Royal Mail and GPL now charge each other for mail delivered to their respective jurisdictions. However as GPL delivers substantially more mail to Royal Mail than Royal Mail delivers to GPL, GPL incurs a significantly higher charge from Royal Mail. In the past it had been possible for GPL to cross-subsidise certain services, in particular local and UK letter post. This is however no longer sustainable and a move to more cost-based pricing is required. In addition the changes by Royal Mail to Pricing in Proportion (also explained in more detail in Section 4) further impacts upon Guernsey postal users.

The DG is therefore consulting on the application by GPL to amend its tariffs with effect from 1st April 2006. In order to consider the full impact of this proposal the DG is inviting all interested parties to submit their written comments to the OUR so that they may be considered in full prior to a decision being made in December 2005. The rest of this paper sets out in more detail the consultation timetable, the background to the application for tariff changes and the OUR's approach to assessing this application.

2. Structure and Comments

2.1. Structure of the Consultation Paper

The rest of this paper is structured as follows:

- Section 3: describes the legislative framework and licensing arrangements which give the DG power to price control certain areas of GPL's postal activities;
- Section 4: provides some background information on GPL's dynamic commercial environment in order to help understand the scale of the changes GPL has experienced since commercialisation;
- Section 5: sets out the OUR's approach to reviewing GPL's proposals; and
- Section 6: Outlines the next steps in the process which will culminate in the introduction of any new prices in April 2006.
- Annex A: GPL Tariff Application (non-confidential extract) – this is the text of GPL's tariff application and is provided as an attachment to this consultation paper for information purposes only.

2.2. Comments

Interested parties are invited to submit comments in writing on the matters set out in this paper to the following address:

Office of Utility Regulation
Suites B1& B2
Hirzel Court
St Peter Port
Guernsey
GY1 2NH

Email: info@regutil.gg

All comments should be clearly marked "**Comments on Guernsey Post's Proposed Tariff Changes**" and should arrive before 5pm on 21st October 2005.

In line with the policy set out in Document OUR 04/01 – "Regulation in Guernsey; Revised Consultation Procedures", the DG intends to make responses to the consultation available on the OUR website. Any material that is confidential should be put in a separate Annex and clearly marked so that it can be kept confidential. The DG regrets that he is not in a position to respond individually to the responses to this consultation.

The OUR would particularly welcome quantitative responses from interested parties that demonstrate how GPL's price changes would affect them (either as

businesses or private individuals) in order to assess the impact of GPL's proposals.

For example the OUR would welcome information on issues such as:

- Demonstration of how a user's demand for postal services would be affected by proposed price changes (i.e. price elasticities of demand);
- Modelling results showing the impact of price changes on a company's financial performance;
- Explanation of the impact of price changes on the company's strategy (e.g. investment and employment levels);
- Historical actual mail volumes and average weights on a quarterly basis (disaggregated by types of products if considered helpful);
- Projected mail volumes and average weights on a quarterly basis (again disaggregated by types of products, if demand for products are likely to vary i.e. total average weights may vary over time).

The DG would therefore encourage respondents to respond fully to the issues raised by GPL's proposed tariff changes and reiterates that any material that is confidential should be put in a separate Annex and clearly marked so that it can be kept confidential.

This document does not constitute legal, technical or commercial advice; the DG is not bound by this document and may amend it from time to time. This document is without prejudice to the legal position or the rights and duties of the DG to regulate the market generally.

3. Legislative and Licensing Background

3.1. Legislation and States Directions

The Post Office (Bailiwick of Guernsey) Law, 2001 provides that a range of postal activities do not require licensing, ranging from personal private delivery to the delivery of court documents and banking instruments². In addition, any postal services that are provided for a price greater than £1.35 (the “non-reserved services”) can also be provided by any person or business without a licence. All services that are provided for a price of less than £1.35 are deemed to be reserved services and this is set out in an Order made by the DG in accordance with section 9 of the Postal Law³.

The Regulation of Utilities (Bailiwick of Guernsey) Law 2001 provides for the States of Guernsey to issue States Directions to the DG in relation to:

- the scope of the universal service that should be provided in the postal sector in the Bailiwick;
- the extent of any exclusive privileges or rights in the postal sector;
- the identity of the first licensee in the postal sector; and
- any obligations arising from international agreements.

In September 2001, the States issued Directions to the DG that required the DG to issue the first licence to provide universal services to GPL. At the same time the States set out the universal service obligation that should be imposed on GPL which is:

“... throughout the Bailiwick of Guernsey at uniform and affordable prices, except in circumstances or geographical conditions that the Director General of Utility Regulation agrees are exceptional:

- *One collection from access points on six days each week;*
- *One delivery of letter mail to the home or premises of every natural or legal person in the Bailiwick (or other appropriate installations if agreed by the Director General of Utility Regulation) on six days each week including all working days;*
- *Collections shall be for all postal items up to a weight of 20Kg;*
- *Deliveries on a minimum of five working days shall be for all postal items up to a weight of 20Kg;*
- *Services for registered and insured mail.”*

Having defined the universal service, the States directed that GPL should be provided with the exclusive right to provide reserved services insofar as this is needed to enable and ensure the universal postal service is delivered. The relevant States Direction states:

“The Regulator shall reserve services to be exclusively provided by the Universal Service Provider to the extent necessary only to ensure the

² Section 1(2) of the Post Office (Bailiwick of Guernsey) Law, 2001

³ The Post Office (Reserved Postal Services) Order, 2001

maintenance of universal service, and shall review and revise the reserved services from time to time with a view to opening up the Guernsey postal market to competition consistent with the need to maintain the Universal Service”.

This legislative structure provides the DG, GPL and the States of Guernsey with a framework similar to that in neighbouring jurisdictions, within which:

- States policy can be articulated in more detail in the form of States Directions; and
- Licence conditions can be developed to provide more detail on the operation of the market.

3.2. Regulatory Framework

In exercising his functions and powers, the DG has a duty to promote (and, where they conflict, to balance) the following objectives⁴:

- a. protect the interests of consumers and other users in the Bailiwick in respect of the prices charged for, and the quality, service levels, permanence and variety of, utility services;
- b. secure, so far as practicable, the provision of utility services that satisfy all reasonable demands for such services within the Bailiwick, whether those services are supplied from, within or to the Bailiwick;
- c. ensure that utility activities are carried out in such a way as best to serve and contribute to the economic and social development and well-being of the Bailiwick;
- d. introduce, maintain and promote effective and sustainable competition in the provision of utility services in the Bailiwick, subject to any special or exclusive rights awarded to a licensee by the DG pursuant to States’ Directions;
- e. improve the quality and coverage of utility services and to facilitate the availability of new utility services within the Bailiwick; and
- f. to lessen, where practicable, any adverse impact of utility activities on the environment;

States Directions to the DG also require him:

- to ensure that the licensee (i.e. GPL) charged with providing the universal service in the postal sector does so throughout the Bailiwick of Guernsey at uniform and affordable prices⁵; and
- to award the exclusive right to provide postal services in the Bailiwick to the extent that such exclusive right is necessary to ensure the maintenance of the universal postal service.

⁴ The Regulation of Utilities (Bailiwick of Guernsey) Law, 2001

⁵ States Resolutions 2001, pages 78-80 (item no 14)

3.3. Licence Conditions

GPL was awarded a licence on 1st October 2001 in accordance with States Directions and was designated by the DG as being dominant in the market for reserved services in the Bailiwick of Guernsey⁶.

Condition 18 of GPL's licence was amended early in 2005 to allow for the DG to price control GPL's USO services (outside the reserved area) where it has been found by the DG to be dominant.

Therefore in accordance with Condition 18.3 of GPL's postal licence, the DG may regulate the prices of a postal licensee where GPL is dominant. The relevant licence condition states:

“The Director General may determine the maximum level of charges the Licensee may apply for Licensed Services Services and/or Universal Services within a Relevant Market in which the Licensee has been found to be dominant. A determination may:

- (a) provide for the overall limit to apply to such Licensed Services and/or Universal Services or categories of Licensed Services and/or Universal Services or any combination of Licensed Services and/or Universal Services;*
- (b) restrict increases in any such charges or to require reductions in them whether by reference to any formula or otherwise; or*
- (c) provide for different limits to apply in relation to different periods of time falling within the periods to which any determination applies.*

In conclusion the DG has the power to directly regulate the prices that GPL charges for services provided within its USO. At the current time GPL has been found dominant within the reserved area (i.e. those postal services provided for a price of less than £1.35 per item).

USO postal services provided at a price of more than £1.35 are not reserved exclusively to GPL limited and therefore other operators can compete and provide such services. However, if GPL is found dominant in this segment of the USO, the DG has the power to price control these services as well. The DG is currently consulting on this issue and anticipates coming to a view on whether GPL is dominant in any other relevant market before the end of this process and any final decision on GPL's tariff application.

⁶ Document OUR 01/16 Decisions under the Post Office (Bailiwick of Guernsey) Law 2001 – Decision Notice and Report on the Consultation Paper.

4. A Dynamic Commercial Environment

GPL operates in an increasingly dynamic environment and the rate of change in the global postal sector was acknowledged by the States and its advisors in the lead up to commercialisation. The June 1998 Billet d'Etat included a Policy Letter from Advisory & Finance ("A&F") on the future arrangements for the provision of electricity, postal and telecoms services within the Bailiwick. The June 1998 Policy Letter included a Joint Report from A&F, and the Post Office Board, the Telecoms Board and the Electricity Board which acknowledged that to varying degrees each of the Boards was operating in dynamic environments with major changes in their technological and commercial environments. Following this A&F commissioned consultancy advice from KPMG in consultation with the Trading Boards and the Civil Service Board to undertake an assessment of the economic impact of commercialisation within the Bailiwick⁷.

KPMG believed that consumers would benefit from the implementation of the commercialisation policy through likely reductions on tariffs and improvements in quality of service, but of particular concern to the States was KPMG's opinion that some, if not all, of the Trading Boards would slip towards a loss making position within five years due to changes in their operating environments. The objective of commercialisation and the establishment of an independent regulatory regime was to ensure GPL would be better able to respond to these external changes and that prices as a result would be lower than would otherwise be the case.

Therefore in order to help consumers and interested parties understand the commercial background within which GPL operates this section describes GPL's dynamic environment as a context for understanding the impact of those changes on the Bailiwick's postal operator and to help inform responses to the issues raised in this consultation paper.

4.1. *Relationship with UK Postal Operator*

The most significant driver for the GPL's application is again a change in the commercial contract between Royal Mail and GPL. In the previous tariff decision in 2004, GPL experienced a fundamental step change in its underlying costs. Historically the Bailiwick's postal consumers benefited from the fact that whilst GPL delivered all mail received from Royal Mail and Royal Mail in turn delivered all mail received from GPL, the companies did not in fact charge each other but assumed that the costs "balanced out". This contractual arrangement implicitly assumed the same volume and type of mail flows in each direction.

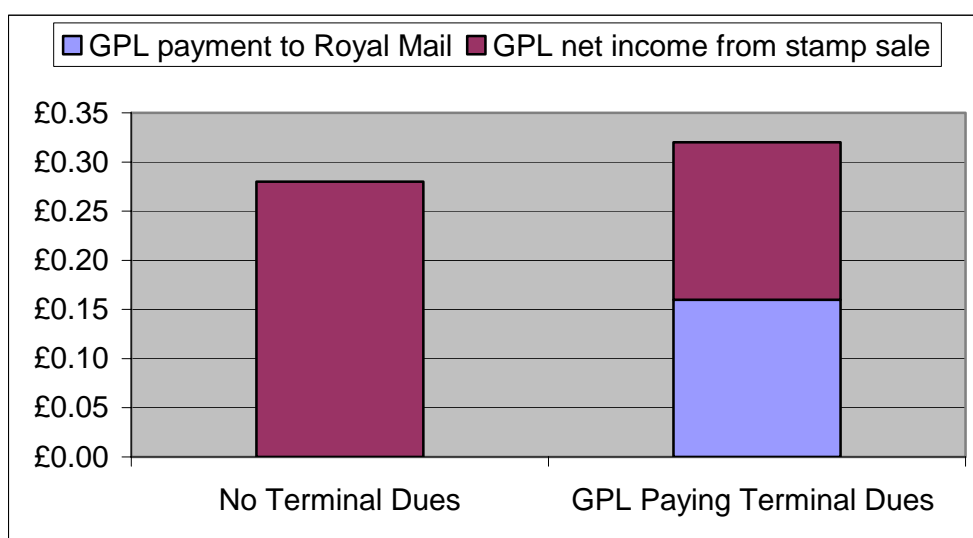
Historically Royal Mail operated on this basis with the three postal operators in Guernsey, Jersey and the Isle of Man. However, there is in fact significantly more mail going from Guernsey to the UK than vice versa. This imbalance has been generated over time as the Bailiwick's economy has grown and attracted direct mail

⁷ Billet d'Etat March 2000

businesses to start up in the Bailiwick. Hence Royal Mail under greater scrutiny through the creation of Postcomm (the UK postal regulator) through the Postal Services Act 2000 and the need to improve its own financial performance could no longer justify subsidizing delivery to the UK of mail from the Bailiwick. In effect Royal Mails' customers had been implicitly subsidizing the Bailiwick's postal customers and the implementation of a proper commercial contract between the two postal operators simply reflected normal commercial arrangements with regard to the payment of terminal dues⁸ between USO providers in two separate jurisdictions.

This commercial arrangement, which sees both Royal Mail and GPL charge each other for the actual volumes of mail in each direction, therefore results in significant increases in charges to GPL for the services provided by Royal Mail and to GPL's underlying cost base. The impact of terminal dues on GPL is illustrated in Figure 1 below.

Figure 1: Hypothetical Illustration of Impact of Terminal Dues Payments for 60g stamp to UK



In this hypothetical example, Figure 1 shows in the first instance GPL's net income for the sale of a 60g letter to the UK where there was no terminal dues payable by the Bailiwick's postal operator. Under this commercial arrangement Guernsey's postal operator would keep 100% of the retail price paid by the consumer who purchased the stamp, i.e. in this example Guernsey's postal operator keeps the 28p and this helped in turn cross-subsidise the cost of the local letter postal services. Essentially, prior to this change, GPL made a significant loss on delivering local letters, but due to the non-commercial nature of its relationship with Royal Mail, it could afford to cover those costs from revenue generated from other postal services.

However in the "GPL paying terminal dues" scenario, GPL has to pay Royal Mail for delivery of the item in the UK. Whilst the methodology for calculating the actual

⁸ Terminal dues are the remuneration postal operators pay to each other for the delivery of cross-border mail in the country of destination.

charge is commercially confidential between the two parties, in this example it is assumed that GPL pays 50% of the retail tariff to Royal Mail for terminal dues. Thus whilst the price of the 60g stamp to the UK may have increased from the original scenario to 32p, GPL's net income would be only 16p with Royal Mail receiving the balance of the retail price. The terminal dues payment can therefore be considered as representing either lost revenue for GPL compared to the past or additional operating costs. As a consequence the cash available to GPL to fund services, such as the local postal service, has been substantially reduced and it is not in a position to provide local services without addressing the underlying costs associated with this and other services.

This section has demonstrated the significant step change in GPL's underlying cost base as a result of the more commercial approach now being adopted by Royal Mail. It has illustrated how closely Guernsey's postal operator is influenced by the actions and behaviour of one its major trading partners. It is therefore worthwhile to consider future forthcoming changes in the UK postal market as these too are likely to have implications for Guernsey in the near future.

4.2. Forthcoming Changes in the UK Postal Market

4.2.1. Price Control Review

Postcomm's current price control review for Royal Mail began in late 2003 and has to date produced three main consultation papers as part of the review. In March 2004, Postcomm consulted on the process, timetable and main issues for the review. In September 2004, Postcomm consulted on setting the principles for the next price control and in June 2005 it consulted on its initial proposals for Royal Mail's next price control⁹.

In summary the proposals would mean that average prices would remain broadly the same over the next four years. Prices for products in a captive basket¹⁰ would change by RPI-3% pa and prices for those services in a non-captive basket could change by RPI-2%.

Postcomm is seeking within its proposals to allow Royal Mail to "rebalance" prices within baskets as it generally supports the principle of cost-reflective pricing. As a result individual prices can rise by up to 4% a year subject to compliance with the average cap for the respective basket. In essence this means that RM could by 2009/10 raise the public tariff first class stamp to 34p and the public tariff second class stamp price to 23p. Increases above these amounts would be possible but would require Postcomm's approval. Postcomm intends to consider the representations received and then issue final which would come into effect from April 2006.

⁹ Postcomm (2005) 2006 Royal Mail Price and Service Quality Review Initial Proposals

¹⁰ Containing those products where Postcomm believes the prospects for competition over the course of the price control are limited or weak. The "non-captive" basket includes those products where the prospects for competition are stronger.

However 2006 will also be important for what Postcomm has called the greatest change in postal pricing since the introduction of the Penny Black. The changes from weight based pricing to Pricing in Proportion (“PiP”) or Size based Pricing (“SBP”) will mean some post will cost less to send than it does now but light-weight items that are also large or bulky will cost more.

4.2.2. Pricing in Proportion

Royal Mail published its PiP proposals on 29 March 2005, revising its original proposals (initially referred to as Size Based Pricing or SBP) which were published in August 2003. Postcomm’s provisional conclusion¹¹ was that Royal Mail’s PiP proposals met the company’s obligations relating to changes to the criteria by which its prices are determined.

Under Royal Mail’s current price control, its PiP changes must result in revenue neutrality i.e. higher prices for some mail items to better reflect costs must be balanced with lower prices for other mail items to better reflect their costs. It would appear that 70% of mail will not experience a price change under Royal Mail’s PiP. Of the 30% of mail items that will be priced differently, about half will be more expensive and half will be cheaper as a result of introducing PiP i.e. the changes in Royal Mail’s prices should not lead to an overall increase in the company’s revenue, but will mean that some customers will pay more and others will pay less.

Postcomm announced on 18 August 2005 that it would accept Royal Mail’s PiP proposals and therefore the way postage is priced in the UK will change to take into account size as well as weight. Mail will fit into one of three categories: letter, large letter and packet. An indication of how the new pricing structure will work is shown in Table 1 below. Considerably more information however is provided on RM’s website.

Table 1: Royal Mail’s Quick Find Information on Size, Weight and Pricing

Format	Size	Weight	Pricing in Proportion		Existing Price Range	
			First Class	Second Class	First Class	Second Class
Letters	Maximum 240 x 165mm 5mm thick	0 - 100g	30p	21p	30p - 46p	21p – 35p
		0 - 100g	42p	35p	30p - £2.71	21p - £2.12
Large Letters	Maximum 353 x 250mm 25mm thick	101g - 250g	61p	53p		
		251g - 500g	85p	72p		
		501g - 750g	£1.23	£1.05		
Packets	Minimum	0 - 100g	94p	80p	30p -	21p - £1.48

¹¹ www.royalmail.com/pricinginproportion.

Format	Size	Weight	Pricing in Proportion		Existing Price Range	
			First Class	Second Class	First Class	Second Class
	353mm long 250mm wide 25mm thick	101g - 250g	£1.19	£1.04	£1.78	
		251g - 500g	£1.59	£1.32		
		501g - 750g	£2.06	£1.66		
		751g - 1kg	£2.53	£1.99		
		1kg – 1.25kg	£4.31 (+ 86p for every extra 250g up to 20kg)			

*These prices are indicative only and are based on Royal Mail's current tariff. The prices shown above are for stamps. Discounts for all franking and account customers on their First Class mail will continue to apply.

Royal Mail has announced that PiP would be introduced from 4 September 2006.

4.2.3. Full Market Liberalisation

Following extensive consultation with stakeholders, Postcomm decided¹² in February 2005 to bring forward the date for full postal market opening in the UK from 1 April 2007 to 1 January 2006. Postcomm decided to do this in a single step, giving RM a nine month extension to the present phase of market opening which was due to end on 31 March 2005. This means that, from 1 January 2006, no part of the postal market will be reserved to Royal Mail alone.

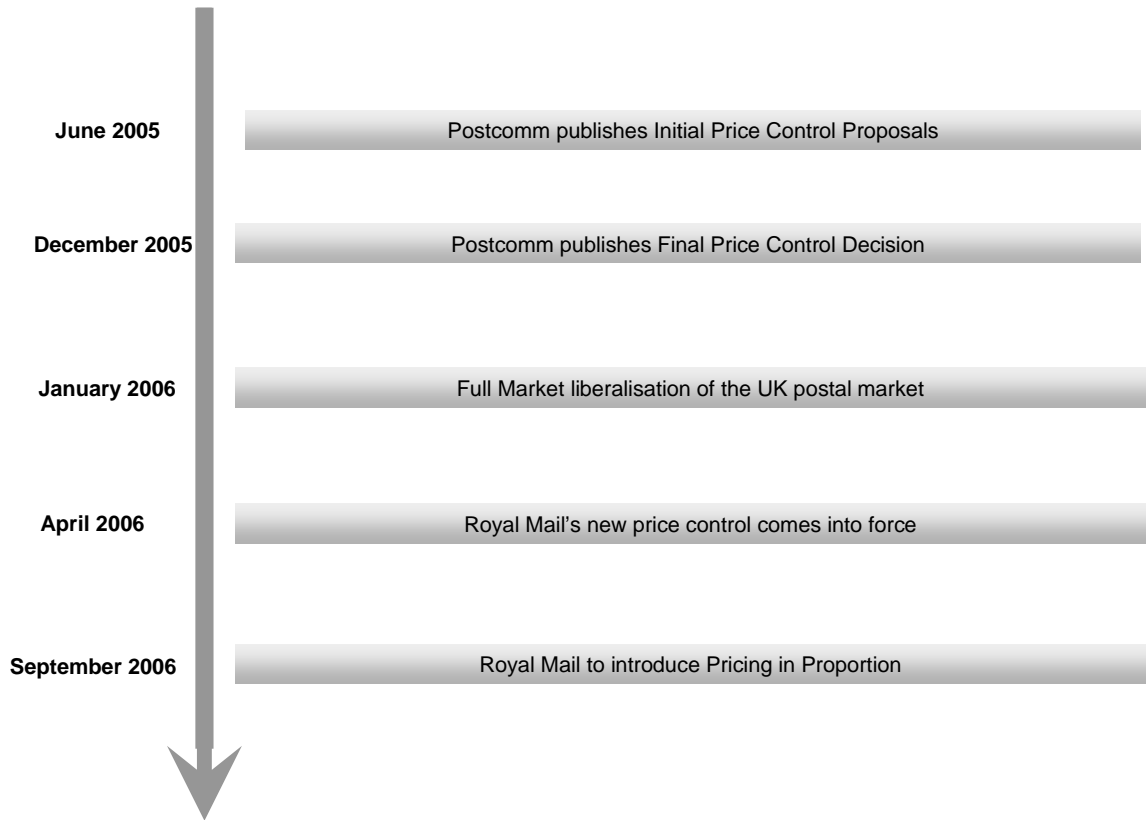
Postcomm believes that advanced full market opening should contribute positively towards sharpening the incentives on Royal Mail to improve its quality of service performance and customer focus.

4.3. Impact on Guernsey's Postal Operator

2006 is going to be a year of significant change within the UK postal market as shown by the culmination of a number of regulatory initiatives as highlighted in Figure 2 below. Some of these changes will represent opportunities for Guernsey's postal market and some will pose threats. The full implications of these changes are not yet certain, but Guernsey will need to be able to respond to these external changes in the coming months. It is possible that the PiP retail prices may have implication for the terminal dues contract between GPL and Royal Mail if this too was aligned with Royal Mail's PiP tariffs. Should this happen then UK bound mail would likely to be affected with light packets facing increases in terminal due costs.

¹² Giving Customers Choice: A Fully Open Postal Services Market. A decision document 18 February 2005

Figure 2 Developments in the UK Postal Market



5. OUR's Approach to Reviewing Tariff Change Application

5.1. Need for a Price Control

In an industry where the incumbent is currently a monopoly and is likely to maintain a dominant position for some time, explicit price regulation is often needed in order to protect consumers' interests. For example, in a monopoly market it is possible for the monopoly firm to act against the consumers' interests through a variety of actions including inter alia:

- absorbing their operational inefficiencies by passing them onto consumers in the form of excessive prices in that there is no incentive to minimize costs;
- setting prices at excessive levels in order, for example to recoup losses made through poor investment or in order to incur monopoly profits.

In the postal sector it is common practice in other jurisdictions across the world for an operator to be granted a monopoly in what is known as the "reserved area" in order to fund the provision of the universal service. Hence as a result of an explicit policy objective there is typically a segment of the postal market in which there is no competition.

In such circumstances regulators have traditionally introduced price controls to ensure that the monopolist/dominant incumbent is not passing unnecessary costs on to consumers and that certain services will continue to be delivered at affordable rates to all sectors of the community. A price control can also ensure that the regulated firm earns an adequate return on its licensed activities and those areas where there is no competition but that, at the same time, it is not unfairly cross subsidising its other activities in competitive markets from the revenue derived in areas where there is no competition

Given the status of the Guernsey postal market, the DG believes that for the legislative and regulatory environment to sufficiently protect consumers' interests, some degree of explicit price regulation and scrutiny of GPL's activities is required.

5.2. Scope for Price Control

The DG considers that the principal criteria for determining the scope of any price control on GPL should include:

- **Protecting consumer's interests by encouraging efficiency and promoting competition wherever possible in the postal sector.** By constraining prices, GPL would be incentivised to search for efficiency improvements in order to satisfy shareholder expectations and earn a reasonable return. In this way a price control can mimic competition and eliminate both excess profits and inefficient practices.
- **Ensuring the provision of the universal service at geographically uniform and affordable tariff throughout the Bailiwick.** By constraining the prices

GPL can charge or the revenues it can earn the DG will need to consider whether doing so would adversely affect GPL's ability to provide such a universal service. The requirement of a uniform tariff may require postal services to be provided at a price below their efficient costs while the same services are provided to other customers at a price above their efficient costs. For example if one customer lives in Sark and the other in Town and they both pay the same amount to send a letter to the Bridge.

At the current time GPL has been found to be dominant in the reserved area and therefore its products within this market are subject to condition 18 of GPL's licence. The DG therefore intends to continue price controlling GPL's prices for postal services within the reserved area. The DG is currently consulting on dominance in a number of other relevant markets and any decision of price controlling universal services outside the reserved area will be made pending the completion of that separate consultation.

The DG notes that GPL has sought in its tariff application for the reserved area to be extended to five times the standard tariff for a 60g UK letter. Under this proposal and GPL's pricing proposal, GPL would have a legal monopoly for all items below a price of £1.70 per item. The DG has the powers to determine the reserved area and can make changes to the determination pending a full consultation. In view of the short duration of GPL's tariff application (see section 5.3) the DG intends to have a more detailed consultation of the appropriate size of the reserved area once this price control has been addressed and an appropriate consultation with interested parties can be undertaken.

5.3. Form and Duration of Price Control

GPL is seeking a one-year tariff change with new prices coming into force on 1st April 2006 through to 31st March 2007. In view of the uncertainty with future direct costs faced by the company the DG believes setting prices for a one year period is appropriate.

The DG is again conscious that GPL continues to face a significant step change in its cost base arising from the new contract with RM, rather than a gradual adjustment of its cost base. Therefore the DG considers that it remains appropriate to consider GPL's proposed tariff change applications on a case by case basis.

5.4. Criteria for Assessing GPL's Proposals

In assessing GPL's tariff proposals the OUR will determine the company's allowed revenues for the price controlled business. This need not correspond to the regulated firm's business in its entirety. The allowed revenues are the revenues required over the period of the price control to cover;

- the price-controlled business's efficient operating cost,
- the price-controlled business's allowable capital expenditure profiles, and
- a return on some measure of the firm's regulatory value.

Once the allowable revenue has been calculated, prices are set at those levels which ensure that the calculated revenues equal the allowable revenues over the price control period. In essence this means that the Net Present Value (“NPV”) of the future cash flows of the price controlled business over the period of the price control, plus the closing asset value of the price controlled business, equal the opening asset value of the price controlled business. Consequently, subtracting the NPV of the future cash flows from the initial asset base will lead to a value of zero (i.e. the price control is NPV neutral). Where this is the case, it means that there is an absence of supra-normal profits and the position is the same as that which would be achieved in a competitive market.

This principle can be expressed in the form:

$$RAB_0 = \sum_0^n CF + RAB_n$$

where:

RAB₀ = Opening Regulatory Asset Base;

CF = NPV of Cash Flows over the price control period, i.e. discounted using appropriate cost of capital; and

RAB_n = Net Present Value of Closing Regulatory Asset Base

In considering GPL’s proposals the DG will be considering in particular the USO requirements for uniform and affordable postal tariffs and the impact of any price changes on different customers. In this context the DG notes that the average household in the UK spends around £26 year on postal services. If Guernsey households have similar consumption patterns as UK households then GPL’s proposed new tariffs would mean domestic customers facing a £2.50 increase in their annual postal expenditure.

5.5. OUR’s Methodology

The OUR is committed to adopting a rigorous, but appropriate, approach to assessing GPL’s tariff change application, taking into account the statutory objectives set out in the Regulation Law. The OUR intends to perform its own analysis and financial/economic modelling exercise using, amongst other information sources, GPL’s confidential Business Plan submitted in support of the tariff changes. However in circumstances where the DG has not been provided with sufficient information or information has not been made available to him, he may need to rely on such other sources as he considers appropriate, such as estimates and benchmarking studies. The DG reserves the right to take all relevant information into account and to adapt the work required to finalise this matter as necessary.

The main activities in the review of the submission will comprise:

- establishing robust estimates of GPL’s efficient asset base and capital costs in order to ensure that customers are not paying for inefficient past investments;
- assessing GPL’s future capital investment programme to ensure that the capital expenditure is economically justifiable;

- reaching an objective decision regarding GPL's cost of capital to ensure that the company earns a reasonable return for its shareholder;
- obtaining the best information possible on GPL's forecast operating costs for its different services and assessing the reasonableness of any forecast efficiency savings, hence ensuring that the company is not passing on inefficient operating costs to consumers in its monopoly markets;
- assessing the reasonableness of the company's postal volume forecasts, taking into account how demand may change in response to price changes;
- forming a view on how the evolution of competition will impact on the GPL's revenues, costs and market share; and
- assessing GPL's provision of a universal service at a geographically uniform and affordable tariff throughout the Bailiwick

The OUR's methodology therefore entails forecasting efficient operating and capital expenditure, including a reasonable rate of return, and setting prices accordingly. Consequently the OUR's determination on GPL's allowed price changes will then be set such that if GPL is managed efficiently, it can expect to cover all its costs, including the costs of its capital employed, over the period of the control.

6. Next Steps

This consultation concludes on 21st October 2005. However, during the course of this consultation the DG intends to have a number of separate meetings with interested parties to discuss issues arising from this paper and GPL's proposed tariff changes. The DG anticipates further information requests and meetings with GPL to understand fully the underlying assumptions and rationale for its tariff change application. Prior to reaching publishing his decision on GPL's tariff application in early December 2005, the DG also expects to conclude the earlier consultation on dominance outside the reserved area within Guernsey's postal market.

ENDS/



**Tariff Submission
for the year
April 2006 – March 2007**

Public Document

Author:
Version Date:

GPL
9th September 2005

1.0 Introduction

Guernsey Post Limited (GPL) has submitted a proposal to revise its regulated postal tariffs from 1st April 2006; the current price control period established by the Office of Utility Regulation (OUR) ceases on 31st March 2006.

The main intentions of this tariff submission are to:

- agree an increase in revenue-generating postal prices to recover increased costs predominantly driven by further substantial rises in the cost of the Royal Mail delivery contract;
- minimise, as far as possible, any significant price shocks to customers whilst Guernsey Post studies the substantial effects of the changes to a Pricing in Proportion (PiP) pricing regime. These tariff proposals start a process of rebalancing, where revenue generated reflects the underlying cost of the product offering. The emphasis is on starting the process rather than achieving this all in one tariff increase because GPL wishes to provide a managed and supported transition to what is expected in 2009¹ by which time Royal Mail will have introduced Pricing in Proportion (details in Appendix One);
- start a process of ensuring that the intention of the Reserved Area (RA) monopoly to fund the Universal Service Obligation (USO) is realised;
- continue to provide a realistic pricing regime for the most commercially competitive aspect of GPL's regulated business, namely the logistics business (Bulk Mailers);

An explanation of how the submission has been presented to the OUR, the commercial logic and timing of the tariffs, the factors that have driven up the costs and the details of the proposed changes are detailed below.

2.0 The format of the tariff submission

GPL has provided, to the OUR, three key documents in order to inform its consultation on, and consideration of, the Company's request to revise its tariffs. These are:

- a financial model that GPL has developed with OUR to best model product revenues and costs and to assess the consequences of tariff structures. GPL has populated this model with historic and budget figures.
- explanatory documentation that:

¹ This is the date when the Royal Mail contract currently being negotiated will terminate.

- establishes the high level product groupings based on their markets;
 - establishes the tariff proposals;
 - provides commercial rationale;
 - demonstrates an efficient asset base and efficient operating costs;
 - explains corporate issues and implications;
 - provides the basis of tariff rebalancing both within product groupings and within the USO and RA.
- this document, an abridged version of the full document described above under point two, but without commercially sensitive information.

3.0 The strategic context of the tariff proposals

3.1 Strategic Plan

The strategy that GPL is operating to, the Strategic Plan 2003-2008², continues in operation, however it has been expanded by a more detailed plan for the Logistics business that has been submitted to the OUR. This plan remains at an early stage and is under constant review in light of external factors.

The opportunities for third party fulfilment operators within Guernsey have been subject to high-level attention from UK and Channel Islands governments. GPL remains committed to growing this sector either through organic growth of existing operators or by encouraging new operators. However GPL will not enter this sector itself, unlike its major competitor Jersey Post, instead supporting the growth of existing third party fulfilment enterprises already operating in the island.

Acquiring new logistics business is not a short-term event and needs to be through a major business relocation decision for the company concerned or the establishment of brand new businesses. It can only be successful where GPL sustains postal prices that are competitive in a global market through it remaining a robust postal operator with a commercial approach to prices.

3.2 A one year tariff proposal – why?

The submission is for a tariff increase that will have a 12-month duration before a further review of funding requirements will drive another submission. The reasons for this are:

- GPL remains in negotiation with Royal Mail to agree contractual terms from April 2006 that will apply both in north - and southbound directions. These negotiations are on-going and have been since October 2004. These tariff proposals must be based on a reasonably assured cost base, approximately seven months before the increase date. Given the status of contract negotiations a sufficient degree of certainty does not exist beyond the first year of the proposed contract.
- The submission in 2003 for a two year price increase which resulted in a single step increase in prices, whilst providing a pragmatic solution to the cost increases

² Strategic Plan 2003-08 submitted as part of the 2003 tariff submission documentation to OUR

being experienced by GPL, did not adequately consider effects of a single large increase over a number of smaller progressive increases. Given the major change in postal tariff regimes that will be led by Royal Mail, i.e. to pricing in proportion (PIP), it is important that GPL's tariff regime does not move out-of-line with competing markets for any significant duration.

- The dynamic situation in the UK postal market continues, with the growth of alternatives to Royal Mail, e.g. TNT and UK Mail. However at this stage they are not positioned to provide services that align to GPL's needs and commitments under its Quality of Service standards at prices that are better than the rates GPL believes it can successfully negotiate with Royal Mail for the first year of its 2006-09 contract. However this area needs to be maintained as an option to develop and establish if appropriate as the UK suppliers mature their services.
- GPL has sought a basket of options for services into the UK from Royal Mail in order to develop new services for Bailiwick customers. Until these are confirmed through a contract it would be inappropriate for GPL to create product offerings for the Guernsey market that align with these options. Furthermore, this cannot be achieved within the timetable of this current submission, hence the preference to have this one-year proposal, effectively a 'holding position' but still achieving some of the longer term price restructuring needs.

4.0 The commercial logic underpinning the tariff proposals

The key factors that have informed the GPL tariff proposals and timing have been the need to:

- recoup the main underlying costs of the business, which are increasingly Royal Mail's charges for the delivery of mail in the UK, and to a lesser extent the conveyance charges of air and sea and the cost of sorting and delivering the mail in Guernsey;
- provide a tariff to the domestic customer that remains affordable but reflects some of the real costs of the postal service on Guernsey and increases the charges GPL can levy on Royal Mail for the real cost of the local operation delivering inward mail from the UK;
- reflect in the UK tariff increasing Royal Mail costs for mail delivery in the UK;
- maintain a competitive tariff for the logistics business;
- provide a tariff for the service sector of the Bailiwick's economy that is comparable with Jersey and UK prices;
- establish prices for the next regulatory price control period starting from 1st April 2006;
- monitor the developing postal market in the UK which is fully liberalised on 1st January 2006 in order to ensure that GPL secures the best deal for mail delivery into the UK for its customers;
- reflect that whilst GPL can predict without excessive uncertainty the rates that will prevail in 2006-07, it cannot realistically ask the OUR, and in turn the posting public, to accept at this stage proposals for the following years that have too uncertain a basis.

5.0 The financial logic underpinning the tariff proposals

GPL has demonstrated transparently to the OUR in the full submission documentation that with the increased costs it incurs through delivery charges outside the Bailiwick there is massive shift in the Company's financial performance into unsustainable loss. GPL's cost budget for 2006-07 has demonstrably been arrived at through a robust and justifiable regime and is in line with the commercial position of an efficient and effective operator.

5.1 The Reserved Area (RA) - £1.35 maximum

The Reserved Area (RA) limit was introduced in 2001 and was equated to 5 times the Guernsey to UK 60g rate, then 27p. This level has not changed since, even though the tariff has now moved to 32p and in this proposal is moving again. Since that time the underlying driver of cost of the UK product, the Royal Mail contract, has seen radical change not least of which in terms of the cost.

GPL believes that whilst the concept of liberalisation within a market is valid – and this is typically achieved through reduction in the RA value – that this is inappropriate in the Bailiwick at this time for the following reasons:

- The increased charges from Royal Mail are unusual and distort the typical liberalisation market where dominant players are not able to control markets. The increase in costs suffered by GPL should be reflected in any RA simply to maintain the entry point to a liberalised market.
- Guernsey has not proved itself to have a postal market of sufficient size that liberalisation can sensibly occur and support more than one operator without resulting in a general lack of viability. This is an assumption taken from lack of movement by the OUR or the States of Guernsey to increase the availability of Postal Licences.
- The effect of the condition 18 revision to extend the OUR price control across the USO services effectively controls GPL to the extent that the OUR can act as if there is an unlimited RA and GPL is subject to quasi-competition within it.

Because of the specific price inflation (Royal Mail charges) in Guernsey's postal market, GPL has proposed to the OUR that it realigns the RA value to the UK 60g postal rate as a mechanism until such time as the abnormal and unpredicted increasing cost base suffered by the Bailiwick is removed and a normal commercial environment exists for postage into the UK. Whilst at this stage few streams of traffic regularly exceed the current value (except all parcels) the necessary commitment to fund the USO should be protected through a logical mechanism.

5.2 Funding Implications

GPL is seeking in its tariff submission to comply with the return envisaged by a regulatory model for its postal controlled business. This is based on the budgets as entered in the financial model and an efficient asset base - which is based on an identified minimum asset base to provide a postal activity.

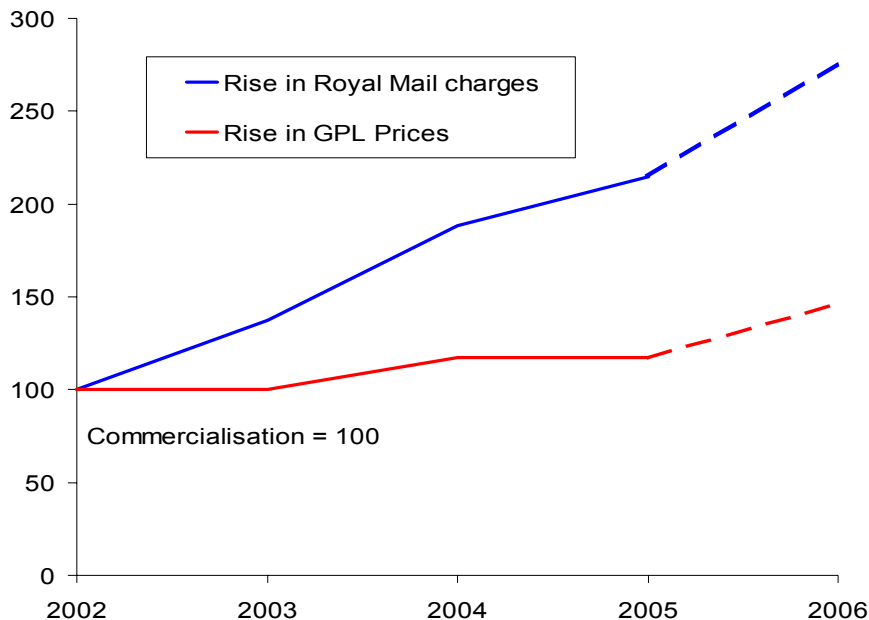
5.3 Dividend and retained profits

The States and GPL deferred the issue of appropriate dividend and profit targets pending the outcome of the NAO review of commercialisation and how the States should manage its shareholdings. The outcome of this report is still awaited.

5.4 Royal Mail charging regime

The details of the contract terms that GPL believes it will conclude with Royal Mail, and have been used in the submission, have been detailed to the OUR in writing but are commercially sensitive. This contract, to the extent that its financial structure exists, has also been modelled and is included as an Excel model submission to the OUR. Fig:1 demonstrates the value for money Guernsey Post has provided through comparison of its public tariff for a typical posted item to the UK against the charges levied by Royal Mail. For commercial reasons the monetary value of this cost cannot be disclosed so the Y-axis takes the cost at the time of commercialisation as 100% with percentage increases reflected against it.

FIGURE 1 : Value for Money : Price



5.5 Retail Network operations

GPL considers that the retail network primarily provides access points for the postal network and the retail activity that can take place should be seen as a cost saving to the postal activity. Particular evidence of this is the operation of sub-Post Offices in Alderney and Sark. Commercially GPL would not wish to operate in these locations from a retail perspective but provides them to ensure postal access points. This follows the logic established by the NAO in its report on the rural post office network in the UK³.

The mechanism applied within the GPL financial model to allocate the cost of the Retail operation has been on a full cost allocation basis, based on the transactional activity at the outlets. Approximately 70-80% of the cost of the network has been recharged to postal products. However there is an argument, developed in its determination on the previous tariff submission by the OUR, that postal pricing should not bear the costs of the network to the extent that they reflect any more than the minimum access point need. Whilst the mechanism applied within the cost model is a full Activity Based Costing (ABC) approach and does not adjust for any network over-specification. GPL believes that the outcome achieved does fully account for this inevitable excess capacity given the density of retail outlets it provides. Any further removal of allowable costs from those applied by GPL would be inappropriate.

The logic of this argument is:

- there is an obligation to provide postal access points within the USO definition, however there is no definition of the density of these access points;
- therefore GPL would use the terms within its Customer Charter as determining the density of such access points. This states an island coverage of a retail facility within a two mile radius of an islander's his home⁴;
- applying the NAO logic that the primary role of the retail network is to provide postal access points and any deficit on this operation is a cost to the postal operation;
- however GPL will accept that it is providing in excess of the terms identified in the Customer Charter, in effect a social commitment or in a specific area a historic anomaly of over-specification. This excess should be funded by GPL either as a reduced return on its activity or through some form of States direct support. The stance being taken by GPL is that it should be the former and this logic has been applied to the proposed level of dividend to the States as shareholder.

6.0 Market review and proposed 2006 tariffs

The approach to letter tariffs has been structured around macro-level product groupings: local mail; standard letter mail to the UK, which includes flower box traffic; logistics operations for bulk mailers; and international mail. There is also parcel traffic to consider.

³ NAO report to DTI 'Financial Support for Post Offices', Appendix H

⁴ Guernsey Post's Customer Charter terms

6.1 Local Mail

The local mail market is defined by three types of customer:

- infrequent social and business customers with social mail and small scale billing/receipting activity;
- the major periodic commercial posters who send large scale bill runs out to almost all delivery points, e.g. Guernsey Water, Guernsey Gas, C&W;
- Royal Mail, who contract with GPL to deliver approximately 16 million items per year.

GPL has used all research available to generate the proposed one year tariff with a headline rate of 29p; an increase of 11.5%. (Details of the proposed new tariff are at Appendix Two). This compares favourably against postal prices in Jersey where local mail, within Jersey alone unlike the universal pricing for the Bailiwick of Guernsey, has cost 33p since April 2005. Indeed the trend in local postal pricing has seen Bailiwick mail priced very competitively compared with Jersey as demonstrated in the trend analysis chart below (fig:2).

This proposed 29p local tariff for the whole Bailiwick also compares favourably against comparative European postal operators, again demonstrated opposite in fig:3. As is standard practice, this proposed new rate would also apply to HM Forces Air Letter Form under their standard terms and conditions.

The expectation with regard to Bailiwick rates is gradual increases to the appropriate level within market-based constraints before 2009 to better reflect the full cost of efficient local operations. This would position GPL such that the most likely (and indeed the default) basis of its contract for international and UK mail delivery in the Bailiwick from 2009, the internationally recognised Universal Postal Union terms, would be based upon a local tariff that realistically relates to the cost of supply. This focus will also drive GPL to seek at its next tariff submission a split of the first weight step. This is currently a single step to 100g whilst a weight step at 60g allows for better alignment with the UPU mechanism.

FIGURE 2 : Comparative 2001-2005 local postal prices: Bailiwick v Jersey

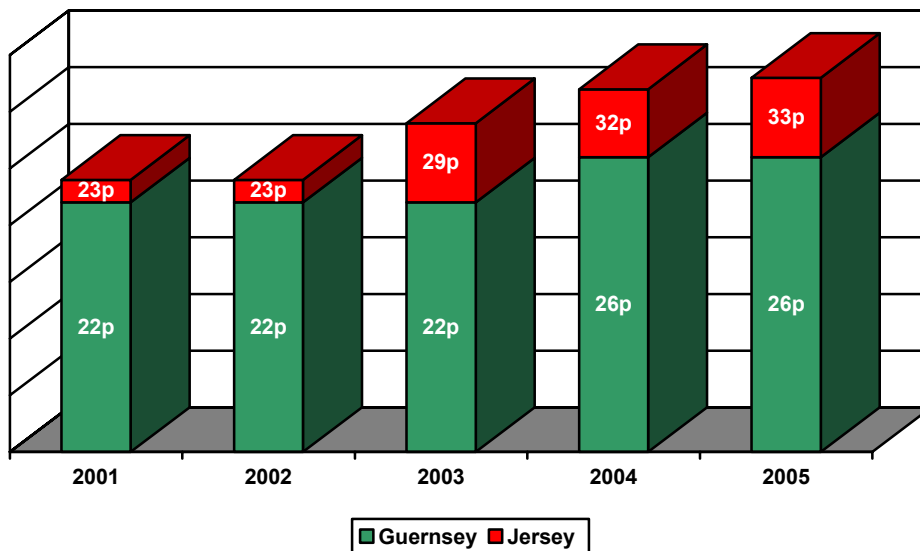
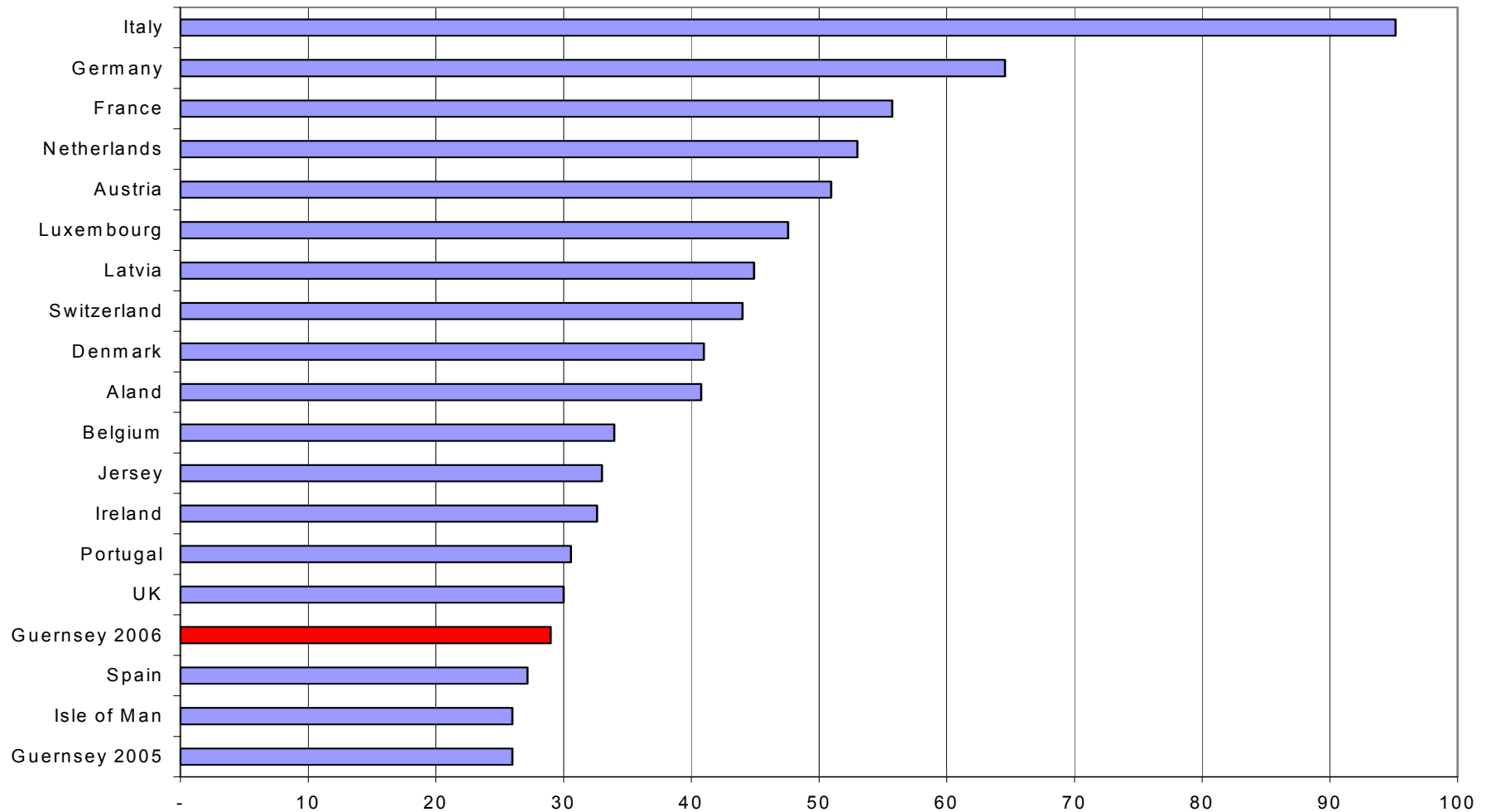


FIGURE 3: Comparison of 2005 prices for 50g local letter



6.2 Standard letter mail to the UK

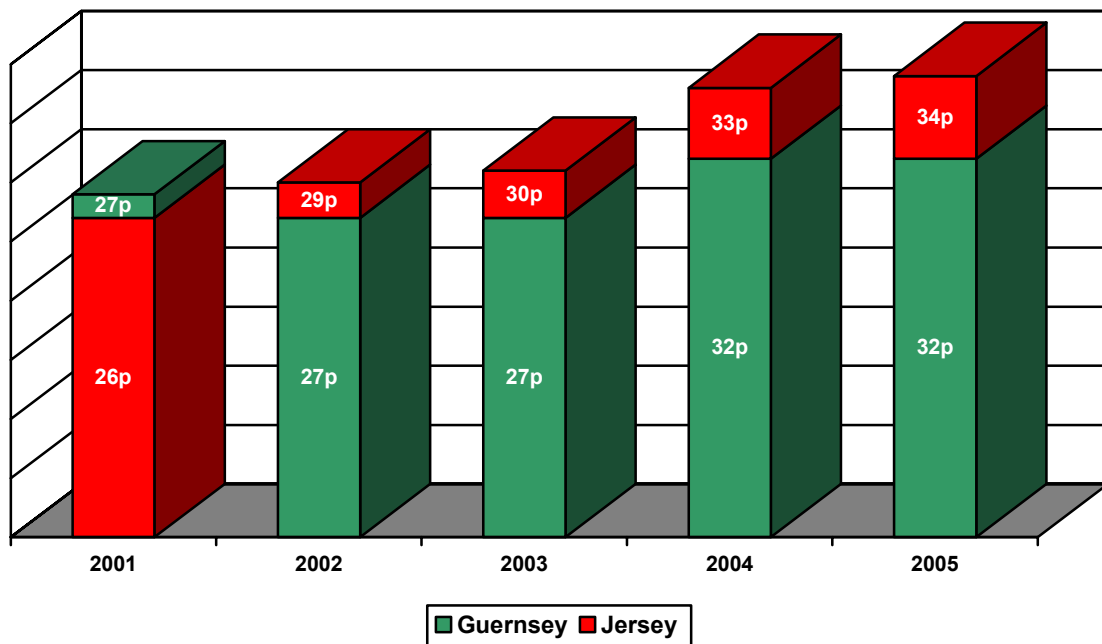
There are again three sub-markets to this market:

- Infrequent social and business customers;
- Large corporate posters, e.g. banks and others within the Finance Sector;
- Flowers-by-post companies, ranging from small operators to substantial ones.

GPL has used all available research to generate the proposed tariff at Appendix Two.

GPL is proposing an increase of 6.3% to the basic tariff, as the price structure in place is expected to reasonably align with costs and the mail profile is similar to that of the mail in the UK, minimising the potential impact from the UK drive to introduce Pricing in Proportion. The headline rate will be 34p with effect from 1st April 2006, equal to that introduced in Jersey in April 2005 (see fig:4 for postal pricing trend chart and fig:5 for European comparative chart).

FIGURE 4 : Comparative 2001-2005 UK postal prices: Bailiwick v Jersey



In the 2004 tariff revision, the favourable volumetric flower box tariff had to be removed due to the significant changes in the basis of Royal Mail's delivery charging which moved from a per item basis to a weight-based charge. Flower mail order companies had to adjust to new weight based pricing. This difficult transition was achieved and the individual operators suffered increases entirely dependant on the weight of the item.

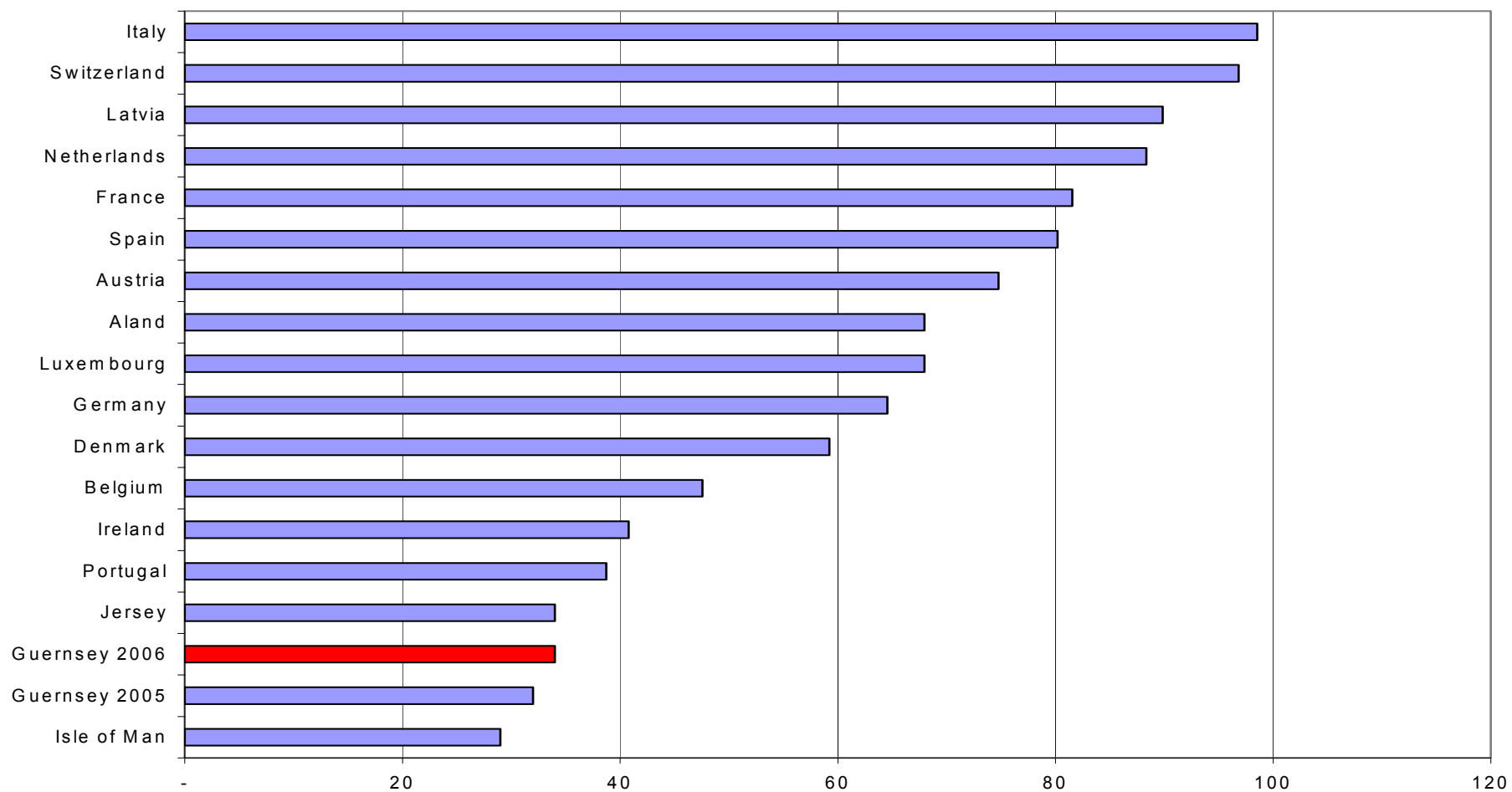
Guernsey Post tariff proposals for the year April 2006-March 2007

As with all postal service dependant industries, GPL has continued to try to keep flower box rises at the lowest possible level to support the States agenda to maintain a diverse economy and encourage its indigenous horticultural businesses on the island. This must, however, be balanced by GPL's need to operate a cost reflective and transparent pricing regime for those products and services within the regulated sector.

By maintaining its weight-based pricing regime, again GPL is delaying the impact of the changes in UK delivery charges for its customers and the reality of Pricing in Proportion is avoided for the current time. Flower boxes are oversized packets and would be charged heavily under full reflective pricing from Royal Mail. This reality will need to be considered by flower-growers and distributors together with GPL before 2009 but GPL has constructed its UK tariff such that flower boxes should see only a 12.9% increase in rates if they continue to use GPL's Straight Line Pricing (SPL) product introduced in 2004. For unsorted non-discounted options, qualifying terms and conditions will remain as they are now i.e. a minimum consignment size of 10 boxes as compared with 100 items for all other letter and letter packet traffic.

Indeed with the size of increase, and the fact that operators in the UK will not be protected from PiP for the period that Guernsey's flower-growers will be, GPL anticipate that Guernsey's flowers export industry will be commercially advantaged.

FIGURE 5 : Comparison of price for 50g letter to UK



6.3 Logistics (bulk customers)

The bulk mail business must be considered in isolation given the complexity of options and reality of cost implications. Due to the un-blending of Royal Mail's prices as a result of its introduction of PiP, the real future impact on mail-order customers' cost base, wherever they operate from, needs to be addressed. As each business operates in a unique market place, GPL has been in discussion with these customers individually on the subject of tariffs and formally sought their input before submitting tariff proposal to the OUR.

Competing against UK prices

The fact is that the Bulk Mailers' profile consists mainly of packets (although given time and restructuring some could move to flats⁵) and the real cost of these has been lost in a blended pricing regime (no format distinction). As PiP is introduced into the UK delivery charges experienced by GPL, the real and significantly higher cost of handling packets will have to be reflected in the posting prices borne by this sector. Through its contract negotiations GPL has tried to provide a delay for Bulk Mailers in arriving at the full impact of PiP. Again GPL does not intend to introduce PiP at this stage, delaying the impact for its customers in order that competitor reaction to changes in the UK can be studied. However it does need to have a pricing regime that reflects the underlying Royal Mail contract.

Additional to the base price are the variations that GPL is offering to Bulk Mailers for levels of sortation. The Decision Notice OUR 04/02A established a tariff regime for Bulk Mailers that included a concept of 'workshare' that created an opportunity to accept certain levels of pre-sortation by Bulk Mailers that had no impact on the GPL tariff but did have on their own costs and Quality of Service (QoS) in delivery time to the UK recipient. GPL has sought to arrive at a menu of sortation and delivery prioritisation options that will allow Bulk Mailers to achieve a lower price that aligns with their own business model and resources, i.e. different levels of sortation going from 0⁶ to 120 way (maximum) and priority(1st class) or economy (2nd class) handling by Royal Mail in the UK.

Competing against the Jersey alternative

Jersey, through its Jersey Post (JP) third party fulfilment operation in particular, provides the natural and local competition to Guernsey in achieving the business of Bulk Mailers. This has been considered within the commercially sensitive document submitted to the OUR.

⁵ Flats and packets are European and UK accepted sizing terms

⁶ The nomenclature of '0' and '120'-way sort are postal terms and do not reflect the actual specification: for no-sort a standard level of splitting into 4 areas is required and for 120 way the current requirement is into postcode sortation levels, as determined periodically by Royal Mail. This detail will be clarified in the terms & conditions for bulk mailers and in consultation document discussions with Bulk Mailers.

The GPL proposals

To obtain best information on expected volumes, profiles and preferred sortation options GPL sought an early input into its planning from Bulk Mailers, by requesting from them individually, details of their volume projections. This approach was supported by the OUR in an attempt to ensure consistency of information from Bulk Mailers to GPL in support of its submission and to OUR to assist in its assessment of GPL's proposals.

GPL is proposing pricing formulae set out at Appendix Two. This follows the SLP mechanism of a rate per item and per Kg that currently exists for Sea Bulk bands A&B. However it has been developed to include tariffs which explicitly reflect the work-share that Bulk Mailers are prepared to undertake and that GPL then avoids in its own costs or its charges from Royal Mail and volume discounts to reflect the reality of the commercial marketplace.

In line with the consultative approach that GPL has been following, all customers will have received details of how exactly GPL believes these proposals will impact them. Additionally senior staff from GPL will be meeting with each client to discuss the specifics still further in order that they can participate as well-informed clients of GPL in the forthcoming OUR consultation on this tariff proposal. It is not appropriate to calculate an average increase for this sector, as has been presented in other sectors, because the impact will differ between clients subject to their individual mail profiles and current tariff arrangements with GPL.

6.4 International tariffs

In its 2004 tariff change, GPL removed the small packet rate. Whilst there has been negative public reaction to the removal of this tariff, the reasons remain valid⁷ and there are no plans to reinstate it. Indeed there is no international product offering currently available for GPL to utilise that provides the same level of service for such a reduced price.

GPL has been presented with a further problem in the uncertainty of the charge structure going forward with international traffic: in many ways GPL is simply the collecting agent for this traffic on behalf of Royal Mail which negotiates all its deals. GPL's international traffic is a miniscule element of Royal Mail's total international operations; direct GPL international negotiations are not appropriate for the volume of traffic. Currently Royal Mail provides all the operational infrastructure of international sortation and logistics from London onwards for regulated product offerings.

Whilst GPL has been receiving a charge for its international traffic based on the UK profile of international traffic, when Royal Mail's London Langley international office is operational, Guernsey mail will be separately identified and GPL will be billed precisely according to its own posted traffic profile. Based on limited data available, GPL and Royal Mail believe that the Guernsey traffic profile is more heavily skewed towards European destinations than for UK profile. This reflects the

⁷ OUR document OUR ¾ - GPL tariff consultation

smaller percentage of population in Guernsey from Asia, Caribbean and Africa than exists in UK and the existence in Guernsey of a high number of European financial institutions. European charges are unfortunately typically higher than other destinations because of their higher local postage rates.

Because of this uncertainty as to implications, and to reflect the agency nature of GPL with regard to international mailings, GPL has tried to mirror rates published by Royal Mail with a premium for Guernsey to UK transfer. This is the first increase in international letter tariffs since May 2000.

GPL expects an increase in its rates when the true profile of its mail is charged and the proposed new tariffs reflect this bias in traffic; European tariffs will increase on average by 20% but those destinations covered by the World Zone 1 and 2 tariffs will increase on average by only 5.7% and 4.8% respectively. This is a very favourable performance against RPI with 25.1% inflation experienced during this period (July 2000 – April 2006).

6.5 Parcels

Based on increased operational costs, a 10% increase in the public tariff for local parcels and a 5% increase for UK parcels and across all zones for international parcels is proposed. RPI is projected to be running at a level of 9.4% April 2004-06

6.6 Other services

The supplemental charges for Signed-for, International Signed-for and Airsure will not increase, nor will air letters and enhanced parcel insurance.

Non-regulated services such as business products Private Boxes and Timed Delivery and Collection; and social services such as Redirection and Keepsafe are not increasing in April 2006.

Appendix 1

Proposed Public tariff changes for 2006

Letters				
Weight (g)	Local to local letter rates		Local to Jersey & UK letter rates	
	Proposed 2006	Current 2005	Proposed 2006	Current 2005
	£	£	£	£
60	0.29	0.26	0.34	0.32
100	0.29	0.26	0.50	0.46
150	0.43	0.38	0.66	0.60
200	0.57	0.50	0.82	0.74
250	0.71	0.62	0.98	0.88
300	0.85	0.74	1.14	1.02
350	0.99	0.86	1.30	1.16
400	1.13	0.98	1.46	1.30
450	1.27	1.10	1.62	1.44
500	1.41	1.22	1.78	1.58
550	1.55	1.34	1.94	1.72
600	1.69	1.46	2.10	1.86
650	1.83	1.58	2.26	2.00
700	1.97	1.70	2.42	2.14
750	2.11	1.82	2.58	2.28
800	2.25	1.94	2.74	2.42
900	2.53	2.18	3.06	2.70
1000	2.81	2.42	3.38	2.98
Each additional 50g	0.14	0.12	0.16	0.14

Guernsey Post tariff proposals for the year April 2006-March 2007

Parcels				
Weight (not over Kgs)	Local to local parcel rates		Local to Jersey & UK parcel rates	
	Proposed 2006	Current 2005	Proposed 2006	Current 2005
	£	£	£	£
1	2.65	2.40	4.30	4.10
2	3.10	2.80	5.25	5.00
4	3.85	3.50	7.15	6.80
6	4.40	4.00	8.60	8.20
8	4.95	4.50	10.00	9.50
10	5.50	5.00	11.35	10.80
15	9.10	8.25	13.25	12.60
20	11.00	10.00	14.70	14.00
30 (max)	13.20	12.00	15.75	15.00

Guernsey Post tariff proposals for the year April 2006-March 2007

Recorded Delivery		
	Proposed 2006	Current 2005
The fee for Recorded Delivery in addition to the appropriate postage	£1	£1

Guernsey Post tariff proposals for the year April 2006-March 2007

Surface Mail		
Weight (not over grams)	Proposed 2006	Current 2005
	All mail (outside Europe only) £	All mail (outside Europe only) £
20	0.38	0.36
60	0.61	0.58
100	0.88	0.83
150	1.23	1.16
200	1.58	1.49
250	1.93	1.82
300	2.28	2.15
350	2.63	2.48
400	2.98	2.81
450	3.33	3.14
500	3.68	3.47
550	4.03	3.80
600	4.38	4.13
650	4.73	4.46
700	5.08	4.79
750	5.43	5.12
800	5.78	5.45
850	6.13	5.78
900	6.48	6.11
950	6.83	6.44
1kg	7.18	6.77
Each additional 50g	0.35	0.33
Max weight	5kg	5kg

Guernsey Post tariff proposals for the year April 2006-March 2007

Postcards		
Location	Proposed 2006 £	Current 2005 £
Europe (outside UK)	0.42	0.36
Worldwide	0.45	0.40

Guernsey Post tariff proposals for the year April 2006-March 2007

Airmail						
Weight (not over grams)	Proposed 2006			Current 2005		
	Europe (incl Eire)	Rest of World Zone 1	Rest of World Zone 2	Europe (incl Eire)	Rest of World Zone 1	Rest of World Zone 2
	£	£	£	£	£	£
10	0.42	0.47	0.47	0.36	0.45	0.45
20	0.42	0.68	0.68	0.36	0.65	0.65
40	0.60	1.05	1.12	0.50	1.00	1.07
60	0.78	1.42	1.56	0.65	1.35	1.49
80	0.96	1.79	2.00	0.80	1.70	1.91
100	1.14	2.16	2.44	0.95	2.05	2.33
120	1.32	2.53	2.88	1.10	2.40	2.75
140	1.50	2.90	3.32	1.25	2.75	3.17
160	1.68	3.27	3.76	1.40	3.10	3.59
180	1.86	3.64	4.20	1.55	3.45	4.01
200	2.04	4.01	4.64	1.70	3.80	4.43
220	2.22	4.38	5.08	1.85	4.15	4.85
240	2.40	4.75	5.52	2.00	4.50	5.27
260	2.58	5.12	5.96	2.15	4.85	5.69
280	2.76	5.49	6.40	2.30	5.20	6.11
300	2.94	5.86	6.84	2.45	5.55	6.53
320	3.12	6.23	7.28	2.60	5.90	6.95
340	3.30	6.60	7.72	2.75	6.25	7.37
360	3.48	6.97	8.16	2.90	6.60	7.79
380	3.66	7.34	8.60	3.05	6.95	8.21
400	3.84	7.71	9.04	3.20	7.30	8.63
420	4.02	8.08	9.48	3.35	7.65	9.05
440	4.20	8.45	9.92	3.50	8.00	9.47
460	4.38	8.82	10.36	3.65	8.35	9.89
480	4.56	9.19	10.80	3.80	8.70	10.31
500	4.74	9.56	11.24	3.95	9.05	10.73
Each additional 20g	0.18	0.37	0.44	0.15	0.35	0.42
Max weight	2kg	2kg	2kg	2kg	2kg	2kg

Guernsey Post tariff proposals for the year April 2006-March 2007

International Signed For		
	Proposed 2006	Current 2005
The fee for International Signed For service in addition to the appropriate postage	£3.30	£3.30

Weight (not over grams)	Proposed 2006			Current 2005		
	Europe (incl Eire)	Rest of World Zone 1	Rest of World Zone 2	Europe (incl Eire)	Rest of World Zone 1	Rest of World Zone 2
	£	£	£	£	£	£
10	3.72	3.77	3.77	3.66	3.75	3.75
20	3.72	3.98	3.98	3.66	3.95	3.95
40	3.90	4.35	4.42	3.80	4.30	4.37
60	4.08	4.72	4.86	3.95	4.65	4.79
80	4.26	5.09	5.30	4.10	5.00	5.21
100	4.44	5.46	5.74	4.25	5.35	5.63
120	4.62	5.83	6.18	4.40	5.70	6.05
140	4.80	6.20	6.62	4.55	6.05	6.47
160	4.98	6.57	7.06	4.70	6.40	6.89
180	5.16	6.94	7.50	4.85	6.75	7.31
200	5.34	7.31	7.94	5.00	7.10	7.73
220	5.52	7.68	8.38	5.15	7.45	8.15
240	5.70	8.05	8.82	5.30	7.80	8.57
260	5.88	8.42	9.26	5.45	8.15	8.99
280	6.06	8.79	9.70	5.60	8.50	9.41
300	6.24	9.16	10.14	5.75	8.85	9.83
320	6.42	9.53	10.58	5.90	9.20	10.25
340	6.60	9.90	11.02	6.05	9.55	10.67
360	6.78	10.27	11.46	6.20	9.90	11.09
380	6.96	10.64	11.90	6.35	10.25	11.51
400	7.14	11.01	12.34	6.50	10.60	11.93
420	7.32	11.38	12.78	6.65	10.95	12.35
440	7.50	11.75	13.22	6.80	11.30	12.77
460	7.68	12.12	13.66	6.95	11.65	13.19
480	7.86	12.49	14.10	7.10	12.00	13.61
500	8.04	12.86	14.54	7.25	12.35	14.03
Each additional 20g	0.18	0.37	0.44	0.15	0.35	0.42
Max weight	2kg	2kg	2kg	2kg	2kg	2kg

Guernsey Post tariff proposals for the year April 2006-March 2007

Airsure		
	Proposed 2006	Current 2005
The fee for Airsure service in addition to the appropriate postage	£4	£4

Weight (not over grams)	Proposed 2006			Current 2005		
	Europe (incl Eire)	Rest of World Zone 1	Rest of World Zone 2	Europe (incl Eire)	Rest of World Zone 1	Rest of World Zone 2
	£	£	£	£	£	£
10	4.42	4.47	4.47	4.36	4.45	4.45
20	4.42	4.68	4.68	4.36	4.65	4.65
40	4.60	5.05	5.12	4.50	5.00	5.07
60	4.78	5.42	5.56	4.65	5.35	5.49
80	4.96	5.79	6.00	4.80	5.70	5.91
100	5.14	6.16	6.44	4.95	6.05	6.33
120	5.32	6.53	6.88	5.10	6.40	6.75
140	5.50	6.90	7.32	5.25	6.75	7.17
160	5.68	7.27	7.76	5.40	7.10	7.59
180	5.86	7.64	8.20	5.55	7.45	8.01
200	6.04	8.01	8.64	5.70	7.80	8.43
220	6.22	8.38	9.08	5.85	8.15	8.85
240	6.40	8.75	9.52	6.00	8.50	9.27
260	6.58	9.12	9.96	6.15	8.85	9.69
280	6.76	9.49	10.40	6.30	9.20	10.11
300	6.94	9.86	10.84	6.45	9.55	10.53
320	7.12	10.23	11.28	6.60	9.90	10.95
340	7.30	10.60	11.72	6.75	10.25	11.37
360	7.48	10.97	12.16	6.90	10.60	11.79
380	7.66	11.34	12.60	7.05	10.95	12.21
400	7.84	11.71	13.04	7.20	11.30	12.63
420	8.02	12.08	13.48	7.35	11.65	13.05
440	8.20	12.45	13.92	7.50	12.00	13.47
460	8.38	12.82	14.36	7.65	12.35	13.89
480	8.56	13.19	14.80	7.80	12.70	14.31
500	8.74	13.56	15.24	7.95	13.05	14.73
Each additional 20g	0.18	0.37	0.44	0.15	0.35	0.42
Max weight	2 kg	2kg	2kg	2kg	2kg	2kg

Guernsey Post tariff proposals for the year April 2006-March 2007

International Standard Parcel								
	Zone 5	Zone 6	Zone 7	Zone 8	Zone 9	Zone 10	Zone 11	Zone 12
weight in kgs	ROI	Belgium, Netherlands, Luxembourg	France, Denmark, Germany	Italy, Spain, Portugal, Greece	Rest of Europe	USA, Canada	Far East, Australia	Rest of World
current 2005 (£)								
0.5	5.40	16.20	16.20	16.20	18.00	15.00	20.70	20.70
1.0	6.55	17.70	17.70	17.70	20.20	18.70	24.35	25.60
1.5	7.70	19.20	19.20	19.20	22.45	22.45	28.00	30.55
2.0	8.80	20.70	20.70	20.70	24.65	26.15	31.70	35.45
2.5	9.95	22.20	22.20	22.20	26.90	29.90	35.35	40.40
3.0	11.00	23.30	23.30	23.30	28.90	33.40	38.60	45.05
3.5	12.00	24.35	24.35	24.35	30.95	36.95	41.80	49.75
4.0	13.00	25.45	25.45	25.45	33.00	40.50	45.05	54.40
4.5	14.05	26.50	26.50	26.50	35.05	44.05	48.30	59.10
5.0	15.05	27.60	27.60	27.60	37.10	47.60	51.55	63.80
5.5	15.65	28.50	28.50	28.50	38.50	50.40	54.25	68.10
6.0	16.25	29.40	29.40	29.40	39.95	53.20	56.95	72.40
6.5	16.85	30.30	30.30	30.30	41.40	56.05	59.65	76.75
7.0	17.45	31.20	31.20	31.20	42.85	58.85	62.35	81.05
7.5	18.05	32.10	32.10	32.10	44.30	61.70	65.05	85.40
8.0	18.65	33.00	33.00	33.00	45.70	64.50	67.75	89.70
8.5	19.25	33.90	33.90	33.90	47.15	67.30	70.45	94.00
9.0	19.85	34.80	34.80	34.80	48.60	70.15	73.15	98.35
9.5	20.45	35.70	35.70	35.70	50.05	72.95	75.85	102.65
10.0	21.05	36.60	36.60	36.60	51.50	75.80	78.55	107.00
10.5	21.70	37.20	37.20	37.20	52.60	77.95	81.20	110.60
11.0	22.40	37.80	37.80	37.80	53.75	80.10	83.80	114.20
11.5	23.05	38.40	38.40	38.40	54.90	82.25	86.45	117.80
12.0	23.70	39.00	39.00	39.00	56.05	84.40	89.10	121.40
12.5	24.35	39.60	39.60	39.60	57.20	86.60	91.75	125.00
13.0	25.00	40.20	40.20	40.20	58.30	88.75	94.40	128.60
13.5	25.70	40.80	40.80	40.80	59.45	90.90	97.00	132.20
14.0	26.35	41.40	41.40	41.40	60.60	93.05	99.65	135.80
14.5	27.00	42.00	42.00	42.00	61.75	95.20	102.30	139.40
15.0	27.65	42.60	42.60	42.60	62.90	97.40	104.95	143.00
per 0.5kg	0.50	0.35	0.35	0.35	0.85	1.70	2.50	3.10

Guernsey Post tariff proposals for the year April 2006-March 2007

International Standard Parcel								
Weight in kgs	Zone 5	Zone 6	Zone 7	Zone 8	Zone 9	Zone 10	Zone 11	Zone 12
Proposed 2006 (£)								
0.5	5.65	17.00	17.00	17.00	18.90	15.75	21.75	21.75
1.0	6.90	18.60	18.60	18.60	21.20	19.65	25.55	26.90
1.5	8.10	20.15	20.15	20.15	23.55	23.55	29.40	32.10
2.0	9.25	21.75	21.75	21.75	25.90	27.45	33.30	37.20
2.5	10.45	23.30	23.30	23.30	28.25	31.40	37.10	42.40
3.0	11.55	24.45	24.45	24.45	30.35	35.05	40.55	47.30
3.5	12.60	25.55	25.55	25.55	32.50	38.80	43.90	52.25
4.0	13.65	26.70	26.70	26.70	34.65	42.50	47.30	57.10
4.5	14.75	27.85	27.85	27.85	36.80	46.25	50.70	62.05
5.0	15.80	29.00	29.00	29.00	38.95	50.00	54.15	67.00
5.5	16.45	29.95	29.95	29.95	40.45	52.90	56.95	71.50
6.0	17.05	30.85	30.85	30.85	41.95	55.85	59.80	76.00
6.5	17.70	31.80	31.80	31.80	43.45	58.85	62.65	80.60
7.0	18.30	32.75	32.75	32.75	45.00	61.80	65.45	85.10
7.5	18.95	33.70	33.70	33.70	46.50	64.80	68.30	89.65
8.0	19.60	34.65	34.65	34.65	48.00	67.75	71.15	94.20
8.5	20.20	35.60	35.60	35.60	49.50	70.65	73.95	98.70
9.0	20.85	36.55	36.55	36.55	51.05	73.65	76.80	103.25
9.5	21.45	37.50	37.50	37.50	52.55	76.60	79.65	107.80
10.0	22.10	38.45	38.45	38.45	54.10	79.60	82.50	112.35
10.5	22.80	39.05	39.05	39.05	55.25	81.85	85.25	116.15
11.0	23.50	39.70	39.70	39.70	56.45	84.10	88.00	119.90
11.5	24.20	40.30	40.30	40.30	57.65	86.35	90.75	123.70
12.0	24.90	40.95	40.95	40.95	58.85	88.60	93.55	127.45
12.5	25.55	41.60	41.60	41.60	60.05	90.95	96.35	131.25
13.0	26.25	42.20	42.20	42.20	61.20	93.20	99.10	135.05
13.5	27.00	42.85	42.85	42.85	62.40	95.45	101.85	138.80
14.0	27.65	43.45	43.45	43.45	63.65	97.70	104.65	142.60
14.5	28.35	44.10	44.10	44.10	64.85	99.95	107.40	146.35
15.0	29.05	44.75	44.75	44.75	66.05	102.25	110.20	150.15
per 0.5kg	0.55	0.35	0.35	0.35	0.90	1.80	2.65	3.25

Guernsey Post tariff proposals for the year April 2006-March 2007

International Economy Parcel				
	Zone 9	Zone 10	Zone 11	Zone 12
weight in kgs	Rest of Europe	USA, Canada	Far East, Australia	Rest of World
current 2005 (£)				
0.5	14.95	13.45	18.70	14.50
1.0	16.50	15.85	21.65	16.75
1.5	18.05	18.25	24.60	18.95
2.0	19.60	20.65	27.55	21.20
2.5	21.20	23.05	30.50	23.40
3.0	22.55	25.15	33.00	25.60
3.5	23.95	27.25	35.50	27.85
4.0	25.30	29.35	38.05	30.05
4.5	26.70	31.45	40.55	32.30
5.0	28.10	33.55	43.10	34.50
5.5	29.35	35.60	45.40	36.40
6.0	30.60	37.60	47.75	38.35
6.5	31.85	39.65	50.10	40.25
7.0	33.10	41.70	52.45	42.20
7.5	34.40	43.75	54.80	44.10
8.0	35.65	45.80	57.10	46.00
8.5	36.90	47.80	59.45	47.95
9.0	38.15	49.85	61.80	49.85
9.5	39.40	51.90	64.15	51.80
10.0	40.70	53.95	66.50	53.70
10.5	41.90	55.80	68.45	55.70
11.0	43.10	57.65	70.45	57.65
11.5	44.30	59.50	72.40	59.65
12.0	45.50	61.40	74.40	61.60
12.5	46.70	63.25	76.40	63.60
13.0	47.90	65.10	78.35	65.60
13.5	49.10	66.95	80.35	67.55
14.0	50.30	68.80	82.30	69.55
14.5	51.50	70.70	84.30	71.50
15.0	52.70	72.55	86.30	73.50
per 0.5kg	1.00	1.80	1.90	1.90

Guernsey Post tariff proposals for the year April 2006-March 2007

International Economy Parcel				
	Zone 9	Zone 10	Zone 11	Zone 12
Proposed 2006 (£)				
0.5	15.70	14.10	19.65	15.25
1.0	17.30	16.65	22.75	17.60
1.5	18.95	19.15	25.85	19.90
2.0	20.60	21.70	28.95	22.25
2.5	22.25	24.20	32.00	24.55
3.0	23.70	26.40	34.65	26.90
3.5	25.15	28.60	37.25	29.25
4.0	26.55	30.80	39.95	31.55
4.5	28.05	33.00	42.60	33.90
5.0	29.50	35.25	45.25	36.25
5.5	30.80	37.40	47.65	38.20
6.0	32.15	39.50	50.15	40.25
6.5	33.45	41.65	52.60	42.25
7.0	34.75	43.80	55.05	44.30
7.5	36.10	45.95	57.55	46.30
8.0	37.45	48.10	59.95	48.30
8.5	38.75	50.20	62.40	50.35
9.0	40.05	52.35	64.90	52.35
9.5	41.35	54.50	67.35	54.40
10.0	42.75	56.65	69.85	56.40
10.5	44.00	58.60	71.85	58.50
11.0	45.25	60.55	73.95	60.55
11.5	46.50	62.50	76.00	62.65
12.0	47.75	64.45	78.10	64.70
12.5	49.05	66.40	80.20	66.80
13.0	50.30	68.35	82.25	68.90
13.5	51.55	70.30	84.35	70.95
14.0	52.80	72.25	86.40	73.05
14.5	54.10	74.25	88.50	75.10
15.0	55.35	76.20	90.60	77.15
per 0.5kg	1.05	1.90	2.00	2.00

Appendix 2

Proposed Logistics tariff changes for 2006

Mail Pricing formulae rounded to 2 decimal places

Bulk Mail tariffs up to 60g	Sortation	Proposed 2006 (p)	current 2005 (p)
UK Bulk Air	0	34.00	32.00
UK Bulk Air	120	30.60	32.00
UK Bulk Sea Priority	120	27.68	32.00
UK Bulk Sea Customs ⁸	0	35.89	32.00
UK Bulk Sea Economy	0	35.09	32.00
UK Bulk Sea Economy	17 ⁹	31.55	32.00
UK Bulk Sea Economy	120	26.78	32.00
Bulk Mail tariffs at 60g			
UK Bulk Air	0	37.20	34.80
UK Bulk Air	120	33.48	34.80
UK Bulk Sea Priority	120	30.29	34.80
UK Bulk Sea Customs ⁸	0	39.26	34.80
UK Bulk Sea Economy	0	38.40	34.80
UK Bulk Sea Economy	17 ⁹	34.52	34.80
UK Bulk Sea Economy	120	29.30	34.80
Bulk Mail tariffs per g above 60g			
UK Bulk Air	0	0.32	0.28
UK Bulk Air	120	0.29	0.28
UK Bulk Sea Priority	120	0.26	0.28
UK Bulk Sea Customs ⁸	0	0.34	0.28
UK Bulk Sea Economy	0	0.33	0.28
UK Bulk Sea Economy	17 ⁹	0.30	0.28
UK Bulk Sea Economy	120	0.25	0.28

Minimum consignment sizes will apply in order to qualify for the sortation tariffs¹⁰

⁸ Bulk Sea unsorted and non-customs cleared - GPL reserve the right to charge a premium for unsorted mail which is not customs cleared, as Royal Mail have also reserved the right to charge GPL for this.

⁹ Subject to agreement with Royal Mail

¹⁰ Mandatory bulk mail contracts with new formal product specifications will apply.

Qualification for Volume Discounts

Discounts per item	No of items	Net Spend	Proposed 2006
Band A	50,000	50,000	5.00%
Band B	500,000	400,000	7.50%
Band C	1,000,000	800,000	10.00%
Band D	2,000,000	1,600,000	12.50%
Band E	3,000,000	2,400,000	15.00%
Band F	4,000,000	3,000,000	17.50%
Discounts per g			
Band A	50,000	50,000	5.00%
Band B	500,000	400,000	7.50%
Band C	1,000,000	800,000	10.00%
Band D	2,000,000	1,600,000	12.50%
Band E	3,000,000	2,400,000	15.00%
Band F	4,000,000	3,000,000	17.50%

Qualifying volumes and net spend will include all bulk mail tariffs (air and sea), but exclude any standard public tariffs.¹¹

¹¹ New Logistics Terms and Conditions will be issued to cover the new tariff regime

Appendix Three

Royal Mail's Pricing in Proportion Tariff Regime

Pricing in Proportion (PiP) will change the way Royal Mail charges for postal items from a system based primarily on the weight of items to one based on both the format and weight of items.

Royal Mail's primary motivation to introduce PiP is that it believes that PiP better reflects the costs of handling mail than the present weight based pricing structure. This is because its costs, especially in sorting and delivering mail items, vary with the format (letters, flats, packets) of the items. Royal Mail has argued that a pricing structure out of line with its costs would frustrate its ability to compete in a liberalised market and hinder its ability to improve its efficiency.

This will generate commercial tariffs that are more closely cost reflective and will mark a departure from the historic position where Royal Mail's behaviour, including its pricing decisions, were subject to non-commercial factors.

The change in pricing regime has been agreed in principle with its Regulator, PostComm, although the results of the price control that establishes the framework for the rates themselves has yet to be determined.

New PiP-based public posting tariffs will be in operation across the UK with effect from 4th September 2006.

The contractual agreements that Royal Mail will now enter with all its customers, including competitors using downstream access and other operators such as GPL, will necessarily also move from a system based primarily on the weight of items to one based on both the format and weight of items.

At this stage of the negotiations, GPL believes it can realistically continue to provide weight-based tariffs for another year and provide the time necessary to monitor the introduction of the new pricing regime into the UK market. Inevitably, however, its contract will reflect PiP and GPL will have to address how best to manage this change to its cost base with those of its customers who will be most greatly affected.

Further information relating to PiP can be found at the following locations:

<http://www.royalmail.com/portal/rm/content2?catId=400105&mediaId=21100324>

<http://www.postcomm.gov.uk/Departments/SubSection.asp?ID=171>

<http://www.neopost.co.uk/index.asp?Page=2724>