

**CWU SUBMISSION TO POSTCOMM CONSULTATION
ON ZONAL PRICING BY ROYAL MAIL**

Introduction

1. The Communication Workers Union (CWU) represents around 250,000 employees in the postal, telecom and related industries. It is the recognised union in Royal Mail Group for all non-management grades, including those responsible for the collection, sortation and delivery of letters and parcels.
2. On 11 September 2006 Postcomm published a consultation document seeking views on the issues that it should take into account when it assesses proposals by Royal Mail to charge large mailers different rates depending on where in the UK their mail is delivered (zonal pricing). Royal Mail applied to Postcomm on 5 July 2006 to introduce zonal pricing to certain bulk mail products used by large mailers such as banks, utilities, advertisers, charities and government. At present Royal Mail charges large mailers the same "one-price-goes-anywhere" rate.

CWU response

3. The CWU has consistently set out our position on the liberalisation of the UK postal market. We have argued that Postcomm's competition agenda is fundamentally in conflict with the primary duty dictated to it by Parliament (to defend the universal service). The rush to full market opening in the UK has allowed rival operators to Royal Mail to 'cherry pick' the most profitable bulk mail services and thereby hit the company's revenues and undermine its

ability to deliver the USO.

4. Allowing private companies to cream-off the most profitable services undermines the simple business model of cross-subsidisation on which the universal postal service depends. Higher weighted items subsidise lower weight items, business users subsidise social users and "local-to-local" mail and deliveries into cities subsidise long distance mail and rural deliveries. This arrangement had worked for the common good and delivered a high quality postal service at lower costs than most comparable European postal sectors. But this complex system of cross-subsidisation which underpins delivery of the USO has now been put at risk as new market entrants target the most profitable parts of Royal Mail's business.
5. As Royal Mail loses market share to entrants who do not have to bear the fixed costs of providing the universal service and who can thus price accordingly (even while Royal Mail is compelled to carry their mail at less than half the price of a first class stamp) so its revenues shrink relative to its costs. Yet it still has to bear all the costs of providing the universal service at a fixed, low price.

Zonal pricing

6. In earlier submissions the CWU has made clear that, as a matter of principle, we are not supportive of zonal pricing. We have consistently and strongly supported retaining the system of cross-subsidisation which has supported the USO for 350 years.
7. But it is now clear that the introduction of full market liberalisation and Postcomm's accompanying regulatory regime is forcing Royal Mail to align its prices more closely to its costs to ensure the company is not exposed to unfair competition. As a result, we believe the introduction of zonal pricing is becoming a growing necessity for the state operator as competition grows across the postal sector.

8. Without such provisions we believe the viability of discharging key aspects of the universal service could, in time, be placed under significant pressure. We would also point out that the failure to align prices to costs would allow Royal Mail's competitors to introduce competition on the basis of false business assumptions which would not be in the interests of the companies themselves in the longer term.
9. Given the requirement on Postcomm to ensure that Royal Mail is able to finance the activities required under the terms of its license, we believe it should accept Royal Mail's proposals to introduce zonal pricing. Doing so would also address the current unfair anomaly whereby other postal operators have the potential to offer lower prices for services to high density areas while the same option is denied to Royal Mail (without the approval of Postcomm).

Summary

10. The CWU has been a consistent critic of postal liberalisation. We have argued that Postcomm's rush to full market opening - which has taken a form and a timetable never envisaged by EU legislation - has put the promotion of competition ahead of its statutory duty to defend the universal postal service.
11. In the past, the USO was supported by a complex system of cross-subsidisation. But this has been undermined by the introduction of an artificial form of competition which allows private operators to 'cherry pick' the most profitable parts of Royal Mail's business. The net effect is to undermine the system of cross subsidies which has supported the USO for over three centuries.
12. In principle the CWU favour retaining the system of cross subsidies and are not supportive of zonal pricing. However, we recognise that the advent of competition is forcing Royal Mail to align its prices more closely to its costs. As a result we believe the introduction of zonal pricing is becoming a growing necessity for Royal Mail as competition grows across the sector.

We thus believe Postcomm should accept Royal Mail's proposals to introduce zonal pricing in line with its application under license condition 21.

RD06/12/191
4 December 2006