

ECONOMIC AFFAIRS PANEL

FRIDAY, 5TH MAY 2006

Postal Incorporation

Panel:

Deputy G.P. Southern of St. Helier (Chairman)

Deputy A. Breckon of St. Saviour (Vice Chairman)

Connétable M.K. Jackson of St. Brelade

Deputy J.A. Martin of St. Helier

Deputy K.C. Lewis of St. Saviour

Witness:

1. Mr. B. Brown, Chief Executive, Jersey Competition Regulatory Authority, in attendance Paul Hamilton and Charles Webb

1. Deputy G.P. Southern of St. Helier:

As you know we are investigating the impact of the change to the fulfilment policy on the potential incorporation of Jersey Post. Before we start the formal hearing I have to read you a statement which defines your position and our position. "It is important that you fully understand the conditions under which you are appearing at this hearing. You will find a printed copy of the statement I am about to read you on the table in front of you. The panel's proceedings are covered by parliamentary privilege through Article 34 of the States of Jersey Law 2005 and as a result you are protected from being sued or prosecuted on anything said during this hearing, although this privilege obviously should not be abused. The proceedings are being recorded and transcriptions will be made available on the Scrutiny website." So, I suppose I ought to start straight in by asking what you see as the benefits that incorporation brings to the postal service.

Mr. B. Brown (Chief Executive, Jersey Competition Regulatory Authority):

I think an important distinction has to be made between incorporation and regulation. Our job, as you are no doubt aware, our principal job under the Postal Services Law is to act as a regulator of the postal services industry once Jersey Post is incorporated, if that is the decision that the States make. That is our primary role and obviously as part of that role we have been preparing in advance for the eventuality of incorporation because if the States do decide to go ahead with incorporation then Jersey Post and any other operator that comes into that certain sector of the market will require a licence. We have primarily been using our time in the run up to incorporation, as far as postal is concerned, in developing the licence which Jersey Post would have on incorporation. So, we have had no real role in assessing the

costs and benefits of incorporation itself, i.e. the decision to move the States out of running the postal services business and to let that be run by a separate company. That is not really within our remit.

Deputy G.P. Southern:

Your role post the incorporation in terms of regulation, what do you see it as?

Mr. B. Brown:

The benefits of regulation, I think, are that we will have a corporatised postal service entity which, at least initially, will continue to have a monopoly in the market place. A de facto monopoly, if not a legal one. The legal monopoly will be removed so as to allow for the scope for competition, where appropriate. But we will, at least in the first stages after incorporation, be faced with the likelihood that Jersey Post will continue to have a very dominant position in certain areas and regulation in that context is intended to act as a surrogate for competition to protect the consumer and promote the consumer's interests in terms of keeping prices down, keeping standards of service up and otherwise protecting the interests of the consumer.

Deputy A. Breckon of St. Saviour:

I think I should declare an interest as we have corresponded on some of the postal matters before. But can I ask you what, in general terms, consultation has been undertaken about the corporatisation and regulation with Jersey Post and other providers?

Mr. B. Brown:

Well, we have been engaged in extensive consultations on the Jersey Post licence itself primarily. That has included consultation on things like the universal service obligations. We are under a statutory duty to go out to consultation before we grant any new licence. We are going through that process and we have received submissions, which we have considered, and we have developed the licence into a form in which in the current circumstances we believe is appropriate to grant to Jersey Post on incorporation.

Deputy A. Breckon:

Do you see that extending to a service level agreement that the public can feel comfortable with?

Mr. B. Brown:

Yes, well the licence contemplates that. There is a provision in the licence - I am not sure if you have got a copy in front of you - condition 15 of the licence deals with service quality standards and what the clause provides is that within 3 months after the licence is granted, i.e. within 3 months after incorporation, Jersey Post will submit to us a plan setting out the target levels for service standards which it will achieve. I am summarising here, we essentially consider that plan, decide whether it is appropriate and we may, if we were happy with those standards, issue directions to Jersey Post to make

sure that those standards are met.

Deputy A. Breckon:

Are you aware of the work of the Guernsey authority, the Guernsey regulator, and the universal service obligations that they have given and also the direction from the States of Guernsey and we have a (... several inaudible words)?

Mr. B. Brown:

Yes, I am aware the OUR has recently published a report following a consultation on these matters. I have to say it is not something I have had an opportunity to read yet, we have had other priorities recently, so I am not aware of the exact content.

Deputy A. Breckon:

Have you any benchmarks in mind at the moment for Jersey Post or is it a case of putting in a submission and (...several inaudible words).

Mr. B. Brown:

Yes, condition 15 specifically refers to international best practice. It says that the licensee shall develop and operate the postal facilities so as to progressively achieve standards in line with international best practice. So as we have done in other areas of regulation, we will be looking at the experience in Guernsey and the experience in the UK and probably further afield in the EU especially for a guide as to what international best practice is in this area.

Deputy A. Breckon:

Just a final question, the States of Guernsey have left some leeway, if you like, to give authority to the regulator, do you think that is a help or a hindrance to a regulator?

Mr. B. Brown:

Authority in what respect?

Deputy A. Breckon:

Well, the States of Guernsey have said that they would direct the regulator in postal matters to (... several inaudible words) service level. Is that help, do you think, or a hindrance to the regulator?

Mr. B. Brown:

I think, under law, it is a political decision primarily. There is a similar provision in the Jersey Postal Services Law which enables the EDC (Economic Development Committee), as it then was, and now the Minister to give directions to the JCRA (Jersey Competition Regulatory Authority) on social and environmental matters. Indeed we have received directions and guidance from the EDC regarding

primarily universal service obligations and those directions and guidance have been transposed into the licence obligations on Jersey Post.

Deputy A. Breckon:

Was that helpful as an exercise, political contact regarding the (...several inaudible words)?

Mr. B. Brown:

What for?

Deputy A. Breckon:

Well, did they put anything in there that was helpful or was it (...inaudible)? Bearing in mind it was a political post --

Mr. B. Brown

Yes, under the Postal Services Law we have 2 primary duties. One is to ensure that users of postal services have the services which they want to the extent reasonably practicable and the second is to ensure that the liability to the State in respect of the pensions fund is repaid. Those are the 2 primary duties. So, when we considered the directions and guidance we had to make sure that we were satisfied that by transposing those into the licence that we would be complying with those 2 duties and we took the view that at this stage at least we would be compliant. That is not to say that that will continue for ever and we may have to review the situation.

Deputy J.A. Martin of St. Helier:

Can I come in there about what you said about 8.2 and 8.1? In the minutes of 3rd September 2003 on the Postal Committee, your predecessor, Mr. (...inaudible) and Mr. Latham, and Mr. Syvret who wrote the paper, the issue was that these were 2 conflicting directions and Mr. Latham and Mr. Syvret were going to go away and consider these again and draw up a paper and a policy and come back to the next meeting. Do you know if this report was ever written, because we cannot find one? How do you see this as being a conflict because one ...

Mr. B. Brown:

On the first question, I do not know the answer to that. If it is considered important I can do some research but, as you know, I have been with the JCRA since October 2004 but I do not know the answer to that question. As to the second question, I think it is a very important point which is the relationship between 8.1 and 8.2 and I think the law is absolutely clear on this as to the priority which 8.1 has over 8.2 in the case of conflict. It is clear from the law that the 2 primary duties under 8.1, in the event of conflict, would take priority over the duty to perform our functions in a manner we consider best calculated to further the interest of users, in particular by promoting competition where appropriate. So,

to take an extreme example - I hope it is an extreme example, and this purely hypothetical - if Jersey Post was able to persuade us that the only way it could repay the liability to the States was to increase its postal charges, thereby prejudicing the interests of users then 8.1(b) would have to take precedence over that under the law. But let us hope that situation will never arise.

Deputy G.P. Southern:

It seems to me that that is a strange dilemma to put you under. I would have thought the person in the street would have thought that JCRA's primary duty was to ensure the interests of the consumer rather than to ensure the loan that has been in --

Mr. B. Brown:

There is another primary duty under 8.1 which does take account of the interest of users, and that is to ensure that users receive the services that they want to the extent reasonably practicable. That is not necessarily a consideration in relation to price. You know, does the consumer want this service, if so, we have to exercise our functions in a way which makes that happen as far as it is practicable to make it happen. That is a separate issue from price. It may be that there will be linkage between the 2 because let us say 8.1(b) became an issue in the future, the ability of Jersey Post to repay the liability to the States, then in practice we may be asked to consider the options of saying: "Well, if some of the services were not necessary or demanded the service levels could be reduced in such a way as to save costs and facilitate repayment." That might be one option. Another option might be, you know, increasing postal charges. But I have to emphasise we are talking in terms of hypothetical situations here. We do not know what circumstances will arise in the future. We will have to take a view based on our view as to how these duties would balance out in light of the particular circumstances at the time.

Connétable M.K. Jackson of St. Brelade:

It leads on, to a certain extent, to a concern that we have and that is the Jersey Post scenario plan suggests that changes to the fulfilment policy which took place in February/March represented a 14 per cent loss in the number of postal items and this may reduce profits to Jersey Post from fulfilment down to around 4.5 million. Do you consider that such a level of profit is excessive?

Mr. B. Brown:

We do not have the Postal Services Law at the moment, Jersey Post is subject, even as a States entity, as any other business is to competition law. Under competition law it is accepted that excessive pricing can be an abuse of a dominant position in certain circumstances but, as I say, first of all we have had no reasonable suspicion that excessive prices are being charged which would contravene competition law. If that suggestion was ever put to us and we decided that we had a reasonable suspicion that excessive prices were being charged then we would have to look, as we are required to do under Article 60 of the competition law, at European competition law for guidance. European competition law says that it is

not a simple matter as to whether a price is excessive or not, you have to look at similar industries in other countries as a benchmark and so on. So, it is very difficult to express a view on that point at this stage.

Connétable M.K. Jackson:

We have got concerns over the cross-subsidisation issue. How would you intend to control that within Jersey Post International, within the limited group of companies, in the light of the assumption made by Jersey Post that JCRA will define the universal service obligations which widely allows profit on postage to cross-subsidise the regional network?

Mr. B. Brown:

There is a provision at condition 24 of the licence on cross-subsidisation, and there is a similar provision incidentally in respect of Jersey Telecom under the Jersey Telecom licence, and it requires the licensee not unfairly to cross-subsidise or subsidise any postal services. Now, clearly, what is unfair or not will depend on the circumstances but I think for the purpose of the discussion today it does seem that the profits from fulfilment, as we understand it, are financing the universal service obligations and I think, as a regulator and given our duties under Article 8.1, we would have to accept that that was permissible to the extent necessary.

Deputy G.P. Southern:

My impression is that the issue of cross-subsidisation is one which is seen in somewhat poor light and yet you are saying that in this incorporation cross-subsidisation is likely to be the norm rather than the exception?

Mr. B. Brown:

Well, I think again under normal competition law principles cross-subsidy is usually only considered to be a problem, or a potential problem, where it is having the effect distorting competition. So, for example, if a dominant company was using profits from an area in which it was dominant or had a monopoly to cross-subsidise areas in which it was subject to competition and the effect of that was to make life difficult for its competitors so that it was effectively leveraging its dominant position to achieve a competitive advantage in other markets, then that would usually be considered - or could be considered - a problem under competition law. Here we are talking about services and it depends how you define the relevant market but, I think, under the Postal Services Law we have these primary duties under Article 8.1 and if profits from fulfilment need to be used to give postal users the services which they want then we have a duty to allow that.

Deputy G.P. Southern:

Can I take you on to the whole issue of competition? We are incorporating presumably in the telecoms market in order that we can introduce competition and, the assumption is, bring prices down as a result

and therefore improve the lot of the consumer. In what way do you envisage that an element of competition, either real or artificial, can be introduced into the postal market? It has been put to us, certainly by Richard Syvret, the advisor on incorporation, that telecoms is probably an appropriate market for competition but postal may not be. The concept is is it an actual anomaly?

Mr. B. Brown:

I think you have to be clear that incorporation is only one aspect of the Postal Services Law and competition, or the possibility of competition, is only one aspect. I think it might be useful to separate out the main elements of the Postal Services Law as we see it. The first is the concept of corporatisation or commercialisation, if you like. The transfer of assets from the States to a newly incorporated company so that that company can run the business on a commercial basis. That is one element. The second element is should that newly corporatised entity be regulated? A separate issue. Or can it be left to its own devices. The third issue is if it is to be regulated, and we have talked about the benefits of regulation earlier, who should regulate it? Should it be the government or should it be an independent regulator such as the JCRA? So, all of these issues are separate from the issue of introducing competition. The final broad concept, if you like, which underlies the Postal Services Law is what is commonly referred to as liberalisation, which is the removal of a statutory monopoly so as to allow for the possibility of competition. So, the Postal Services Law has all these elements and I think it is important to bear that in mind. You have got to look at competition law and competition in the context of these other purposes of the Postal Services Law. Coming to the point about competition, the States has decided clearly that it wants to remove Jersey Post's legal monopoly to allow for the possibility, depending on how the market plays out, of competition. Now, whether competition takes root and, if so, how vigorous it is remains to be seen. That depends on the market. But the decision, as I see it, which has been made - I cannot speak for the States, I am just going by my interpretation of the law - is that we want to create the conditions whereby if the market is ripe for competition there is no barrier to entry, apart from requiring a licence if it is within the licensable area. We do not see a need for a statutory monopoly any longer. We want market forces to dictate whether there should be competition and to create the possibility of that competition.

Deputy G.P. Southern:

In the sense that you have examined the market, where would you see that competition arising?

Mr. B. Brown:

We have not conducted a detailed review because that has not really been part of our role to date. Our role has been to prepare the licence which would be issued to Jersey Postal on incorporation. In common with other regulators there is a principle that as far as possible you should let the market decide, you should not try to pre-empt the market. If a licence application were to come in then we would have to go out to public consultation. We would have to assess a number of things in deciding whether to grant a licence. First and foremost, as with our other statutory functions, we would have to

say: “Well, if we grant a licence how does that stack up with our duties under 8.1?” Those are the primary duties. So as part of that we would have to certainly look at the impact which the new licence would have on Jersey Post’s business and its ability to repay the States. Perhaps 8.1(a) would not be such an issue because in circumstances where a new operator was coming into the market that is probably likely to increase the likelihood the customers’ demands are going to be satisfied rather than negate it. So, that would be the first consideration. Now, assuming we were happy that we could issue a licence to the new entrant in a way which was compatible with our 8.1 duties, we would then say: “Okay, well let us look at 8.2, is this going to promote competition?” That would be an important consideration. But before that it would be would it further the short-term or long-term interests of postal users? So you would go through the 8.2 issues and see whether the grant of a licence, and on what terms, was compatible with those duties.

Deputy K.C. Lewis of St. Saviour:

Can I just come in on the assets and liabilities? Could the JCRA confirm the level of assets held by Jersey Post? Has the figure been used as the basis for the assumption that incorporation will be successful?

Mr. B. Brown:

I believe we do have a figure from the 2005 annual accounts. I have got a copy of the accounts here but no doubt the panel has already seen that. Whether that figure has been used as a basis for a view as to whether incorporation would be successful goes back to my earlier point that this is really not something that is within the JCRA’s remit. This is really for the States, I think, so that question would have to be put to the States rather than the JCRA.

Deputy G.P. Southern:

But the figure that you are working on now in terms of your 8.1 duty and viewing that would be the figures from the 2005 accounts? A liability somewhere in the order of 17.8 million under pensions.

Mr. B. Brown:

Under Article 8.1 and Article 8.2 the key thing the sufficiency of financial resources. Under Article 8.1 is whether Jersey Post has sufficient financial resources to meet its liability to the States. Now that is separate from the question of the value of the balance sheet, the net asset position. So as long as we are satisfied that there is sufficient financial resources to repay that liability then that is good enough for us in terms of compliance with 8.1(b).

Deputy G.P. Southern:

Again, if I can return you to the question we were talking about previously about profit levels and when you might intervene in terms of regulation. It has been put to us that, for example, on an asset of

something of the order of - depends what figures you look at - 10- 12 million in terms of assets that proposed fulfilment postage profits, which are uniquely propping up the post office profits of the order of about 4.5 million, is an excessive return on that level of asset and given that return it is almost incumbent on you to intervene in some way. Producing that level of profit from that asset implies that this is tested profit and there should be some form of competition or some form of regulation, limitation, on those profits. Now, there are 2 ways to do that, one you can introduce an artificial level of competition which will say: "You will have to cap your prices because you are making this wonderful profit." The other would be to introduce some real competition and it seems to me that since the profit making area is fulfilment that that is likely to be in fulfilment. If someone, Deutsche Post perhaps, one of the fulfilment companies themselves were to apply to engage in postal operations in the fulfilment area would you see that as the natural competition that might ensue down the line?

Mr. B. Brown:

I think most regulators would say that competition is the best way of making sure that consumers interests are followed through quality of service and prices rather than the regulator seeking to basically impose price caps and so on. I think it remains to be seen whether any prospective operator wants to apply for a licence to engage in this activity. If they do then, again, we have to go through the 8.1 and 8.2 duties and assess under 8.1(b) the impact on Jersey Post's ability to repay the loan. But provided that was okay and provided it is consistent with our other duties under the law then we may want to consider giving them a licence. But, as I say, we have to, under law, go out to consultation on any prospective licence. We will be listening to the views of all interested parties, Jersey Post, Consumer Council, consumers directly and so on before we make a decision. But if we do not receive an application for a licence or we receive an application and we decide not to grant one then we still have our regulatory powers and powers under competition law, where appropriate, to make sure that excessive prices are not being charged.

Deputy A. Breckon:

Can I ask you in your sort of shadow function in respect of Jersey Post if you have had a level of disclosure of information, financial information on post service and things like that? Are you in a position to make sense of where they are at the moment and how things have changed, say, in the last 3 or 4 years by information you have been given?

Mr. B. Brown:

As I said, our primary role in this pre-incorporation period has been to essentially develop the licence and the licence conditions which would be imposed on Jersey Post following incorporation. As part of that process, under Article 8.1(b), we have had to look at financial information to make sure that the terms of the licence that we are proposing to grant will not jeopardise Jersey Post's ability to repay its liability. We are satisfied that a) Jersey Post has given us the information that we felt that we needed for

that purpose and b) that the licence in its current form is consistent on the basis of the information we have with our duties under 8.1 and 8.2.

Deputy A. Breckon:

Can I ask you now more specifically if you noted any change in the pension situation provision? Has there been anything that you would consider dramatic?

Mr. B. Brown:

That really falls outside our remit. I think that is something that concerns the interest of employees and, as such, it would not fall within our --

Deputy A. Breckon:

No, I mean, the liability. The actual sum involved. Have you noticed from the figures you had any changes to that and the way it has been treated?

Mr. B. Brown:

As I understand it the liability is now to repay 4 million over 5 years. That is, if you like, a less onerous position, or a shorter term position at least, than what was initially proposed. So, to that extent, and given that Jersey Post's results under its 2005 accounts appear to have improved on the 2004 results, I think against that background we are particularly satisfied at this stage that the licence is compliant with 8.1(b).

Deputy A. Breckon:

Is there any earlier evidence that you had that conflicted with that? Was there any bigger numbers aside from the pension liability?

Mr. B. Brown:

In terms of the liability of Jersey Post to the States and the sums that were proposed at an earlier stage we had concerns as to whether the liability could be met from areas other than fulfilment. Essentially you pointed out the importance of fulfilment to the business and that is why, if you look at the licence, you will see that there is a condition whereby all of the businesses of the company performed by Jersey Post have to be under the ownership and control of Jersey Post Limited, including the fulfilment business. That is there so, to the extent necessary, the profits from fulfilment can be used to finance the universal service obligations.

Deputy G.P. Southern:

In reducing the loan from 9 million over 9 years - that I believe it was originally - to 4 million over 4 years, certain assumptions were made, for example, there was a reduction in the forecast working capital

of 1.7 million and there was a change to the funding basis for the pension liability on to a normal rather than a high improvement basis. Are you happy with those adjustments?

Mr. B. Brown:

Yes. We took a view when we finalised the licence based on the information that we had at that point under the earlier financing proposal that provided the Jersey Post structure was such that the fulfilment business would be controlled by Jersey Post, we would have no problem in granting the licence under Article 8.1(b). So we had no problem at that stage subject to that condition and subject to the other conditions in the licence obviously. To the extent that that position has now improved then clearly we are even happier.

Deputy G.P. Southern:

We have now got a 4 million loan and that is covered in your duties by 8.1(b), after 4 years - assuming all goes well - that loan is paid off and 8.1(b) falls. What is your position then? Your position then is to ensure that postal services are delivered and that the level of service is such that it meets consumer needs?

Mr. B. Brown:

Once Article 8.1(b) disappears the Postal Services Law will be very similar to the Telecoms Law and there is no equivalent of 8.1(b) in the Telecoms Law. So we will be able to, as a regulator, perform functions in the same way as we are doing in telecoms. Obviously the 2 industries are very different and the scope for competition is probably considerably different but legally we would be on a par with our role as regulator of telecoms.

Deputy G.P. Southern:

There is almost a smile on your face, and you would much happier with that position it seems to me. In fact in these 4 years this double bind that you are in is actually restricting your scope as a regulator.

Mr. B. Brown:

To the extent that it is an additional primary duty that we are subject to and clearly it does leave us less discretion.

Deputy G.P. Southern:

I had a question in front of me and it has just gone again. Nobody is going to rescue me. I know what I was going to talk about.

The Connétable of St. Brelade:

Can I just come in on the JCRA's long-term (...inaudible) because clearly the fulfilment industry is a

high velocity industry which is almost changing monthly at the moment and we have the potential for the British Government to turn the whole thing upside down with very short notice. Would you envisage that Jersey Post would be able to stand up and provide the local delivery requirements given that the fulfilment industry were to reduce profits considerably?

Mr. B. Brown:

The 2005 accounts, as far as I can see, do not attribute a specific figure to fulfilment but, as we understand it, the effect of abolition of LVCR (Low Value Consignment Relief) will have a significant impact on Jersey Post's profits and may even make them marginal. Now, I think in that sort of scenario if there is a proposal to abolish LVCR I think we would be concerned about, first and foremost, 8.1(b) if it happened before the loan had been repaid because that has to be a concern under Article 8.1. In that sort of circumstance I imagine that Jersey Post would probably be coming to us pretty sharpish. But, in any event, we would engage in a dialogue with JP to see how they were proposing to meet that liability. There is a provision in the licence which reflects 8.1(b) whereby they are under a duty to ensure the loan is repaid under the licence. So it would maybe be a concern that we would have about possible compliance with that provision in those circumstances.

The Connétable of St. Brelade:

The only way out really would be for JP to have to renegotiate the loan repayments with JCRA or ...?

Mr. B. Brown:

That would be a matter for Jersey Post.

Deputy A. Breckon:

Have you seen the cost of the regulations? Is that predictable or is it if you had to investigate matters?

Mr. B. Brown:

We have been asked to give a commitment on this issue to Economic Development, according to our best estimates, we have given a commitment that we will use our best endeavours to restrict our costs to 1 million over the next 4 years. That may be slightly frontloaded in the early years. Experience has shown that it tends to decrease as the years go on. But clearly that is an estimate. That is our best endeavours commitment and it is subject to the fact that we have to comply with our legal duties. We have given an indicative estimate as to what our costs are likely to be over the next 4 years and we have said that we will use our best endeavours to keep within those limits, subject to compliance with our legal duties.

Deputy G.P. Southern:

You have obviously been given access to the full accounts and annual reports of the Jersey Post over the

last few years, can you see, from your perspective, any reason why those reports should not have been made available to the States as were previously? Why they should be deemed commercially sensitive at this stage? What in the incorporation process makes that commercially sensitive?

Mr. B. Brown:

Well, our concern has been to ensure that we have access to sufficient information to perform our functions and we are happy, as I said, that we have received that. Whether Jersey Post considers these matters unsuitable for further disclosure on the grounds of the perceived harm it would cause to the business is really a matter for them, I cannot really comment on that.

Deputy G.P. Southern:

If I can return to the original report of that cost benefit on incorporation, I am sorry to press you on this but it is my job. You are obviously aware of the cost benefit analysis done in 2003, at the previous public hearing the independent advisor, Mr. Syvret was asked on a scale of 0 to 10, where 10 was cut your right arm off to incorporate, in 2003 what score would you give and he said between 0 and 3. How would you react to that relatively lukewarm, low score?

Mr. B. Brown:

I do not think I am in a position to comment on that, first of all because the costs and benefits of commercialisation and corporatisation of Jersey Post are really a matter for the States and not for the JCRA. Incorporation, as I mentioned before, is only one aspect of the Postal Services Law. Liberalisation, regulation, competition are other aspects. So I am really not in a position to comment on that.

Deputy G.P. Southern:

Having discovered the figures in 2005, which you did not have access to in terms of costs benefit in 2003, when asked again: "What happened to your score in 2005?" He said: "It went lower." It comes down, I think, to the cost, the opportunity cost, of getting that monopoly. While you are a monopoly and you are in the position to make those profits that is all coming, if you like, back into Jersey Post and through Jersey Post into the States. If, on incorporation, that monopoly profit is placed at risk either by regulation or by real competition that is the reality. How do you feel at this stage about proceeding with incorporation?

Mr. B. Brown:

I think the choice between whether it is better to have a situation where there is a monopoly with all of the profits from the business going to the States and ultimately to the Jersey public in general or whether it is better to have a competitive market, or at least the possibility of a competitive market, with a business which is run separately from the States with the perceived advantages that that may bring, that

balance, I think, is a political decision which I do not think I have a view on.

Deputy G.P. Southern:

Okay. If I could pin you down a little bit if I can. In the 2003 cost benefit analysis we received a report that the JCRA suggested that a small increase in GDP (Gross Domestic Product) of 1 per cent normally occurs when competition is introduced into any market. Could you refer me to any evidence that that is the case? Is that a view you still hold?

Mr. B. Brown:

Yes, I think as a competition authority it is axiomatic that in market economies competition is the best way of promoting economic growth and enhancing GDP. That is the reason why competition has been introduced worldwide, where it has been introduced. It is precisely to further economic growth and GDP. But these are, if you like, qualitative judgments rather than quantitative ones. I do not know what evidence the previous chairman of the JCRA was using for that percentage but I think the important thing is the principle which is that where you have a market economy and the possibility of competition, competition is perceived to be the best way of improving economic growth and that is why we have competition and a competition model. It is a value judgment rather than a judgment based on facts and figures.

Deputy G.P. Southern:

It is rather axiomatic in principle?

Mr. B. Brown:

Yes. I daresay that studies could be done based on prior evidence but, as I say, I am not sure what basis the previous chairman was using for that figure.

Deputy G.P. Southern:

I may be leading you - although I am sure you are adept at not being lead - nonetheless it seems to me that you are saying while in principle we are introducing competition where is that competition going to come from and you are saying, "Well, the market will decide." It does not seem to me very likely that we are going to get any real genuine competition. Would you agree with that or not?

Mr. B. Brown:

It is very difficult to predict what the level of interest will be and the possibility of competing within the licensable area of £1.30 and 500 grams. There is competition outside those areas already and presumably there will continue to be competition. So, we are talking essentially about the prospect of competition within the £1.30 and 500 limit because that is the only area where people need a licence to operate. As a competition authority we can see the possibility of competition, possibly not in local

deliveries. It may be difficult to imagine a scenario where someone could duplicate the distribution system that Jersey Post has but there may be other areas where competition could take root. But we have our own views on that and I think it would inappropriate for me to comment in the presence of Jersey Post on what we see as the prospects. But, in theory, you can see that there could be the prospect of competition in certain areas.

Deputy G.P. Southern:

You seem to be indicating that the asset of Jersey Post is its postmen.

Mr. B. Brown:

I am sorry?

Deputy G.P. Southern:

The one of the major assets of Jersey Post is its postmen on its rounds, you know, they would do the last mile.

Mr. B. Brown:

Yes, in a sense it is analogous to the incumbent telecoms operators who have the last mile access to the customer but that does not mean to say that there is not any prospect of competition in the market.

Deputy G.P. Southern:

But competition there can occur on technological grounds. It seems to me that that is not the possibility with Jersey Post. Again, I put it to you is it not the case that Jersey Post is a natural monopoly?

Mr. B. Brown:

I do not believe that Jersey Post's business as a whole is an actual monopoly, no. I believe that there is a possibility of competition in certain areas. What level of competition it will be remains to be seen. It is difficult to project that.

Deputy G.P. Southern:

At the risk of annoying you, the last point from me before I come back to everybody else, in terms of that 2003 report comparisons were made with much larger scale operations, New Zealand Post or, I think, Deutsche Post itself and talked about major cost advantages, efficiency advantages of those sort of processes, but then immediately said: "Of course it would not be realistic to transfer those possible advantages to a relatively small operation like Jersey Post." Again, in terms of competition and in terms of efficiencies, how much efficiency can you realistically expect from the incorporation of Jersey Post given its scale?

Mr. B. Brown:

We do not know because we have not done the efficiency audit yet. If you look at our aims and objectives for this year one of our first tasks very soon after incorporation could be to conduct a detailed efficiency audit of Jersey Post and we have lined up consultants to help us in that process. It is a very intensive and detailed review and we will be able to assess in the light of that audit what precisely the scope for efficiencies are and if it is appropriate and we think there is scope for efficiencies then we can impose a price capping mechanism to give Jersey Post an incentive to keep its costs to a minimum.

Deputy A. Breckon:

Just a question I would like to ask as we are getting near the end, it is about quality of information you received. In your sort of shadow role are you content that you can start identifying things now, say like (...inaudible) profits and things like that or is the detail not conclusive at this stage?

Mr. B. Brown:

At this stage, because we have no formal regulatory role vis-à-vis Jersey Post, our regulatory role as regulator will kick in after incorporation. At that stage we will have full information gathering priority to assess Jersey Post's profitability and costs and so on by law and it is on that basis that we are able to go in and conduct a detailed efficiency audit.

Deputy A. Breckon:

Would it be true then to say that you are not in a possession of that at the moment?

Mr. B. Brown:

We are not in possession of sufficient information to make a judgment on that.

Deputy K.L. Lewis

Following on from Deputy Breckon's previous question, is the JCRA aware that at the year end 2005 the pension liability for Jersey Post was valued at 17.9 million and that figure in the opening balance of 2006 was 15.3 million? Can the JCRA explain the change in estimate?

Mr. B. Brown:

The short answer to that is no. We have not had a need to question the basis of what is presumably an actuarial valuation. I think the valuation of the pension fund is not a matter that we can legitimately consider. It does not fall within our remit. Our remit covers the sufficiency of Jersey Post's resources to meet its obligations, both to the States and under its licence.

Deputy J.A. Martin

Yes, just to be quite clear on the 8.1 and the 8.1(b). If somebody came to you for a licence in the first 4

years that could maybe offer the same service, maybe slightly cheaper so Jersey Post would not be able to meet their loan repayments to the States, you would have to turn the better offer down to meet that 8.1?

Mr. B. Brown

It would not be a simple assessment. We would go out to consultation. Our main concern would be to examine whether the grant of that licence would, in reality, jeopardise Jersey Post's ability to repay the loan. It is impossible to give a decision in advance on that. We would not be legally entitled to give a decision in advance. It would depend on who the prospective entrant is, what precise area of the business they wanted to compete in, and what impact that was likely to have on Jersey Post's profitability. What contingency plans, what other businesses Jersey Post may be engaged in in order to compensate for any loss of revenue, etc, etc. There would be a whole set of different factors we would need to look at but, as I said, hypothetically at this stage, according to the law, if there was a conflict, if our conclusion was that that the grant of the licence to a prospective new entrant would, after detailed consideration, jeopardise Jersey Post's ability to repay the loan under 8.1(b) then we would have to say no.

Deputy J.A. Martin:

Say no. So that answers really which comes first. I should probably definitely know this, if you refuse a licence is there any place that the licensee can appeal to?

Mr. B. Brown:

Yes, if it believes that there is legal grounds to do so it can go to the Royal Court. But that would have to be based on an argument that we had failed to comply with our duties under the law.

Deputy J.A. Martin:

Thank you.

The Connétable of St. Brelade:

Just to go back briefly to your comment about the detailed efficiency audit of Jersey Post, do you envisage that after that you will flag up areas where competition may be introduced in those traditional fields like (...inaudible) which Jersey Post has undertaken in the past?

Mr. B. Brown:

I think to answer your question it is possible to the extent that certain areas appear to be particularly profitable. Generally speaking the more profits that can be made in a particular sector the more likelihood there is of new competitors who want to get a slice of the action, as it were. But beyond that it is difficult to say. It is difficult to imagine how the level of profitability could nevertheless (...)

inaudible) assess the likelihood and the extent of the prospective competition in the market.

Deputy G.P. Southern:

Thank you for your time and thanks for the information. I hope I was not too pressing.