



Office of the Director of  
**Telecommunications  
Regulation**

**CONSULTATION PAPER**

Regulation of Postal Services  
Approach to Monitoring Compliance  
with Universal Service Tariff Principles

**Document No:** ODTR 01/35

**Date:** 14/5/01

**Oifig an Stiúrthóra Rialála Teileachumarsáide**

**Office of the Director of Telecommunications Regulation**

Abbey Court, Irish Life Centre

Lower Abbey Street, Dublin 1, Ireland

Tel. +353 1 804 9600 Fax. +353 1 804 9680 E-mail [info@odtr.ie](mailto:info@odtr.ie)

# Contents

<b>CONTENTS</b> .....	<b>1</b>
<b>FOREWORD BY DIRECTOR</b> .....	<b>2</b>
<b>1. INTRODUCTION</b> .....	<b>3</b>
1.1. SCOPE OF CONSULTATION.....	3
<b>2. BACKGROUND</b> .....	<b>4</b>
2.1. UNIVERSAL AND RESERVED SERVICES .....	4
2.2. TARIFF PRINCIPLES – LEGISLATION .....	6
2.3. TARIFF PRINCIPLES - DEFINITION .....	7
2.4. INTERNATIONAL PRICE COMPARISONS .....	8
<b>3. THE “AFFORDABLE PRICES” PRINCIPLE</b> .....	<b>12</b>
3.1. PURPOSE OF THE “AFFORDABLE PRICES” PRINCIPLE .....	12
3.2. A TRANSPARENT AFFORDABILITY BENCHMARK.....	12
3.3. REQUIREMENTS FOR AN AFFORDABILITY BENCHMARK.....	13
3.4. CPI–X AS AN “AFFORDABILITY” BENCHMARK .....	14
3.5. SCOPE OF AFFORDABILITY BENCHMARK .....	15
3.6. STRUCTURE OF TARIFF BASKET .....	16
3.7. PROCESS FOR SETTING AFFORDABILITY BENCHMARK.....	17
<b>4. THE “GEARED TO COSTS” PRINCIPLE</b> .....	<b>18</b>
<b>5. GEOGRAPHICALLY UNIFORM PRICES</b> .....	<b>19</b>
<b>6. INDIVIDUAL AGREEMENTS WITH CUSTOMERS</b> .....	<b>20</b>
<b>7. THE “TRANSPARENT AND NON-DISCRIMINATORY” PRINCIPLE</b> .....	<b>21</b>
<b>8. MONITORING COMPLIANCE WITH THE TARIFF PRINCIPLES</b> .....	<b>22</b>
<b>9. SUBMITTING COMMENTS</b> .....	<b>22</b>

## Foreword by Director

In February I published an Information paper [ODTR 01/09] about postal regulation and the consultation procedures I have put in place. This paper is one of three papers I am publishing to ascertain the views of interested parties about the key issues that will form the framework for postal regulation in Ireland.

An Post is at present the only designated universal service provider in the State. It is required to provide postal services<sup>1</sup> for correspondence etc up to 2 kilogrammes, and postal packages up to 20 kilogrammes, and for registered and insured items. It also has a statutory monopoly over reserved services, under weight and price thresholds of 350 grams and £1.50 (five times the basic tariff) respectively.

Efficient and cost effective postal services are an essential element of the infrastructure needed by businesses and individual citizens. A key issue that has to be dealt with is the level and structure of An Post's tariffs, particularly for services where prices are not constrained by competition. The approach chosen must provide effective protection for consumers and others against excessive and anti-competitive pricing, while enabling the company make decisions within an appropriate and stable framework.

I look forward to the responses to this consultation so that there can be clarity as to how the key terms "affordability", "geared to costs", "uniform tariffs" and "transparent and non-discriminatory tariffs" should be applied.

Etain Doyle,  
Director of Telecommunications Regulation.

---

<sup>1</sup> "postal services" means services involving the clearance, sorting, transport and delivery of postal items;

"postal item" means an item addressed in the final form in which it is to be carried by the universal service provider. In addition to items of correspondence, such items also include, for instance, books, catalogues, newspapers, periodicals and postal packages containing merchandise with or without commercial value;

# 1. Introduction

The EU “Postal Directive”<sup>2</sup> establishes a harmonised regulatory framework for postal services throughout the European Union and for securing improvements in the Quality of Service provided, and defines a decision-making process regarding further opening of the postal market to competition. It was transposed into national law last September by the European Communities (Postal Services) Regulations 2000 (SI No.310/2000 “the Regulations”). Under these Regulations the Director has been given responsibility for regulation of the postal sector.

Under Regulation 10 An Post, as the only universal service provider, is required to comply with a set of “tariff principles” for the “universal services” it is required to provide, and under Regulation 18 the Director is required to monitor An Post’s compliance with these principles. The Director’s approval is also required for price increases for reserved services.

In carrying out her functions under the Regulations, the Director is obliged to take into account the views of interested parties. Information Notice ODTR 01/09 sets out her procedure for taking these views into account.

The Director is now undertaking a consultation on how she should approach ensuring that An Post comply with the tariff principles.

The Director would welcome comments from interested parties in relation to any of the questions raised in sections 3 to 8. The closing date for receipt of comments is Friday 15<sup>th</sup> June 2001. Please see section 9 for details on submitting comments on this paper.

## 1.1. Scope of consultation

The Director is consulting on the way in which she will carry out her duties:

- to monitor compliance by An Post with the tariff principles set down in the Regulations to be applied by universal service providers, and

---

<sup>2</sup> Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service. OJ L 15 21.1.1998, p. 14

- to consider any applications for price increases for reserved services.

A stable and effective regulatory framework requires clarity in the Director's interpretation of the tariff principles. A key purpose of this consultation is to achieve such clarity.

The Director will analyse the comments received, take them into consideration, and intends to issue a report on the consultation / decision notice in July 2001.

The Director will subsequently develop the details of her approach, and begin monitoring An Post's compliance with the tariff principles in the provision of the universal service. Should anyone wish to bring relevant matters to the Director's attention, in order to assist with her monitoring obligations, they should do so in writing. If it is required that such information be held in confidence, the relevant sections should be marked as confidential and/or commercially sensitive as applicable.

The Director intends to have these tariff principles to guide her in dealing with any future application by An Post for a tariff increase for reserved services. This approach is without prejudice to the legal position of the Director or her rights and duties under legislation.

## **2. Background**

### **2.1. Universal and reserved services**

The regulatory framework defines the type of postal service that everyone has the right to receive. It covers letters and postal packages up to 20 kilogrammes in weight. Universal service providers must guarantee one clearance, and subject to derogation, one delivery to the address of every natural or legal person in the State five days a week. The Regulations also require universal service providers to provide certain minimum facilities and to comply with directions in relation to quality of service and tariff principles.

The Regulations have designated An Post as a Universal Service Provider and the Minister for Public Enterprise may designate one or more additional postal service providers as a Universal Service Provider having an obligation to provide all or part of the Universal Service.

Regulation 6(5) requires An Post to provide a universal postal service with the following minimum facilities:

- (a) *the clearance, sorting, transport and distribution of postal items up to 2 kilograms;*
- (b) *the clearance, sorting, transport and distribution of postal packages up to 20 kilograms;*
- (c) *services for registered items; and*
- (d) *services for insured items within the State and to and from all countries which as signatories to the Convention of the Universal Postal Union declare their willingness to admit such items whether reciprocally or in one direction only.*

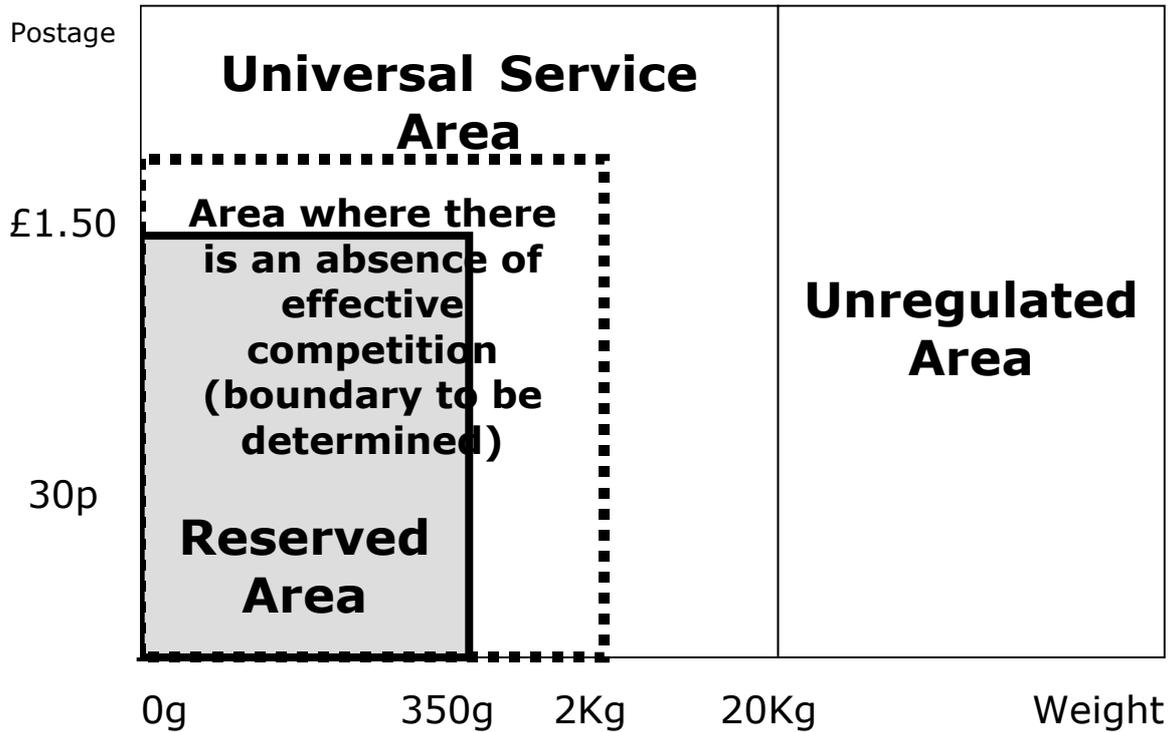
Under the Regulations An Post as a universal service provider has a statutory monopoly over the reserved services. Regulation 9 defines the reserved services as *“the clearance, sorting, transport and delivery of items of domestic correspondence, cross-border and direct mail, whether by accelerated delivery or not, the price of which is less than five times the domestic public tariff for an item of correspondence in the first weight step of the fastest standard category [currently, £1.50], provided that they weigh less than 350g”*. Document exchange is not reserved.

The interrelationship between universal services, reserved services and unregulated<sup>3</sup> services is illustrated in figure 2.1. It should be noted that while the area where there is an absence of effective competition is wider than the reserved area the precise boundaries have to be defined (see section 3.5). Some papers published by the European Commission suggest that there might be some de facto competition for outgoing cross-border mail within the reserved area.

---

<sup>3</sup> ie not subject to the Regulations. Other national and international laws may be applicable.

Figure 2.1. Interrelationship between Universal, Reserved and Unregulated Letter and Parcel services



The level of aggregation of services at which the tariff principles can be monitored depends on the accounting data available – see Consultation paper “*Universal Postal Services - Accounting Separation & Costing Methodology Proposed Direction to An Post*” ODTR 01/29 for proposed definition of “service” in this regard.

## 2.2. Tariff principles – Legislation

The Regulations do not make express provision for a system of ex-ante price regulation of the universal service. Instead, price regulation is based on a set of tariff principles, which operates as follows:

First, An Post is obliged to set its tariffs for all universal services so as to comply with the following tariff principles, set out in Regulation 10(1):

- (a) *prices must be affordable and must be such that all users have access to the services provided;*

- (b) *prices must be geared to costs;*
- (c) *with the consent of the Minister, the Director may decide that a uniform tariff shall be applied throughout the State;<sup>4</sup>*
- (d) *the application of a uniform tariff shall not exclude the right of An Post to conclude individual agreements on prices with customers; and*
- (e) *tariffs must be transparent and non-discriminatory.*

Second, the Director is obliged to monitor An Post's compliance with the tariff principles, and where she is of the opinion that a universal service provider is not complying with the principles can issue directions under Regulation 10(2) (after consultation with the Minister) for the purposes of satisfying the requirements specified in the tariff principles.

And third, the Director's approval is required for any price increase for a service that is reserved to An Post. This power derives from the Postal and Telecommunications Services Act, 1983, as amended by Regulation 4(1), which transfers the power to the Director and restricts its scope to reserved services. No objectives other than compliance with the tariff principles are set for the Director in deciding whether to approve a proposed price increase for a reserved service.

### **2.3. Tariff Principles - Definition**

The "affordable" and "geared to cost" principles provide a framework for the Regulators activity on tariffs.

On the one hand costs are to be "affordable". There is a common sense meaning for this term, although no further clarification is given in the EU Postal Directive or in the Regulations transposing it into national law. It is clearly intended to keep a downward pressure on prices.

On the other hand tariffs are to be "geared to costs", a quantifiable measure which, depending on the costs incurred in providing any particular service, could put either upward or downward pressure on the prices charged for a particular service.

---

<sup>4</sup> The Director has not made such a decision to date.

In practice the “geared to cost” principle will tend to provide a “floor”. As such it is of most relevance to the universal services that are open to competition.

The “affordable cost” will tend to provide the “ceiling” above which customers would be discouraged or even prevented from using the post. It is of most relevance to the reserved services where the absence of competition provides an opportunity for service providers to charge above normal economic levels. There is an expectation that profits earned from the provision of services in the reserved area will be used to finance the extra costs of meeting the universal service requirement in the sectors open to competition. An Post will of course be aware that if prices rise too high business customers will come under pressure to seek alternative communication media, which in turn will lead to reduced volumes for An Post. This is one of the reasons why the reserved area has been set as broadly as it has – the costs of meeting the universal service obligation can be spread over a large number of “reserved items” minimising the impact on unit costs.

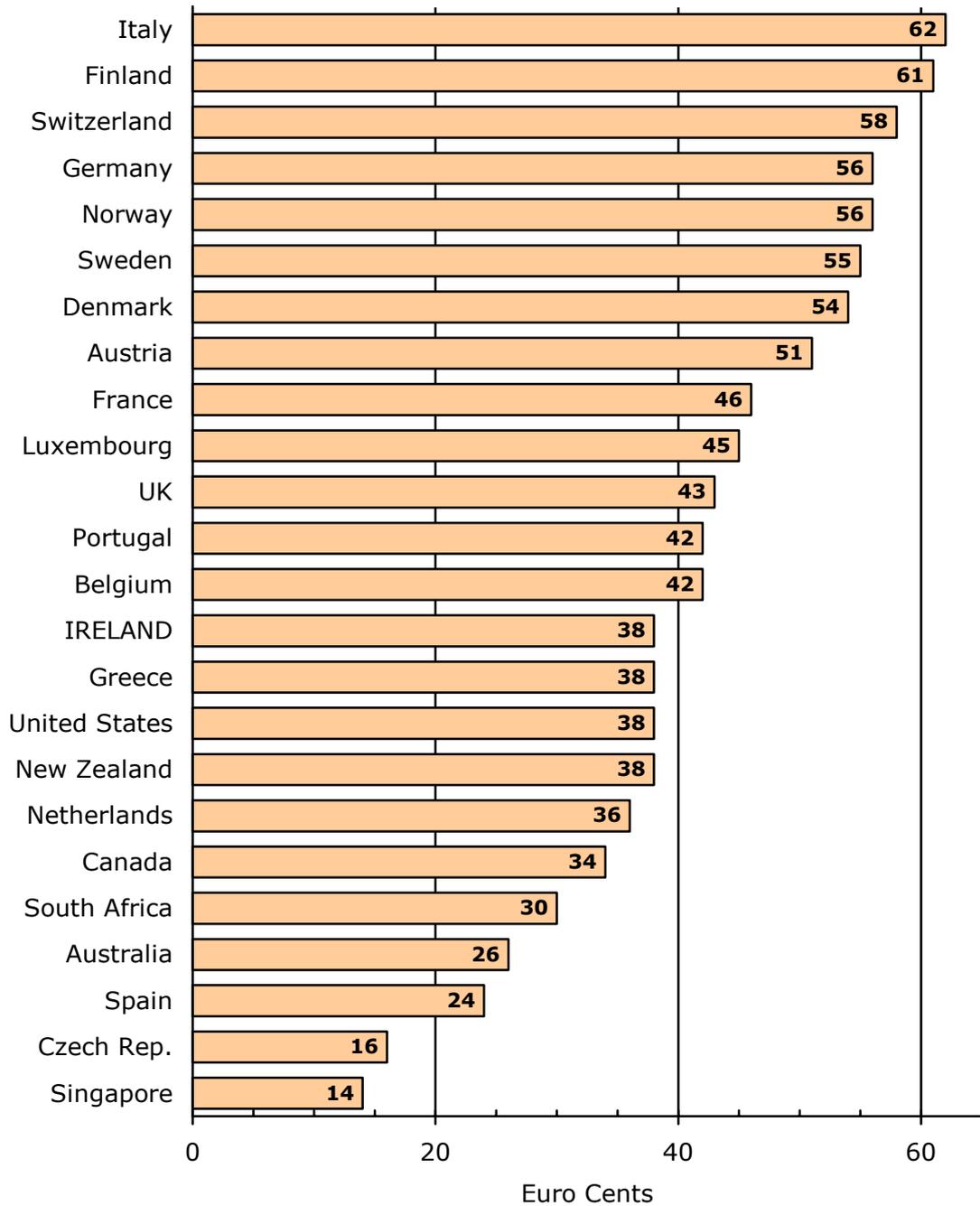
Normally any price can be expected to fall between the “floor” (geared to costs) and the “ceiling” (affordable). But circumstances could arise where the “floor” is higher than the “ceiling”, eg if the service provider was so inefficient that its costs were too high, or if efficiencies of scale were lost as a result of declining volumes.

The Director intends that the application of the principles, taken together, will ensure that the universal service provider is efficient in its operations and that its tariffs will be set accordingly.

#### **2.4. International price comparisons**

Figure 2.2 illustrates how the price of the basic stamp (the “public tariff for an item of correspondence in the first weight step of the fastest standard category” used as reference in the Regulations) varies between the different countries of the European Union and selected other countries.

**Figure 2.2. International Price Comparisons**



Source of data is primarily websites of the relevant Postal Administrations.

Whilst the choice of exchange rate methodology<sup>5</sup> may have an impact on the conclusions, figure 2.2 shows that, of the countries surveyed, only three European Union countries (Spain, the Netherlands, and Greece) offer services at comparable or better prices than An Post, but that on a world-wide basis An Post is near the average.

This analysis, however, takes no account of the many other factors that may influence both the supply and demand of postal services. It does not therefore provide robust information on the relative affordability of postal services in different countries.

Differences in the product offered in terms of the quality of service, the weight and size limits, the extent to which uniform pricing applies and the presence of de facto competition would appear to be significant factors which should be taken into account. Comparative data is provided in Table 2.1 on page 11 .

---

<sup>5</sup> In order to undertake international price comparisons, foreign costs and prices need to be converted into Euro. A number of options are available for the exchange rate to be used in making an international comparison including the nominal market exchange rate; purchasing power parity (PPP) rate, the exchange rate for which a basket of consumer goods costs the same in both countries (price parity); and GDP parity rate, which equalises GDP per head (as a proxy for income). Other options would include input price parity rate, the exchange rate that produces price parity for a basket of input prices (such as land, labour, equipment, etc). For the purpose of this comparison the nominal market exchange rates on 3 May 2001 have been used.

#### **NOTES TO TABLE 2.1**

- # In the first weight step of the fastest standard category in Euros.
- A Fixed Euro exchange rates
- B Exchange rate as at 03.05.01 (mid point spot market)
- C Aspect ratio means that length divided by height must be between 1.3 and 2.5

Source of data is primarily websites of the relevant Postal Administrations.

**Table 2.1 Difference in product offered for Basic Stamp**

Country	Domestic public tariff #	Weight Limit	POP Size Limits (if applied)	Uniform prices	De facto competition in local areas	Economy service available
Spain	24 <sup>A</sup>	20g	Yes	Yes incl. Andorra Gibraltar	Yes	
Australia	26 <sup>B</sup>	250g	240 x 130 x 5	Yes		
South Africa	30 <sup>B</sup>	2kg	220 x 110 x 5	Yes		Yes
Canada	34 <sup>B</sup>	20g	245 x 150 x 5	Yes		
Netherlands	36 <sup>A</sup>	20g	380 x 265 x 32	Yes		
New Zealand	38 <sup>B</sup>	20g	235 x 120 x 20	Yes	Yes	Yes
United States	38 <sup>B</sup>	1 oz = 28.4g	11½" x 6¼" x ¼" plus aspect ratio <sup>C</sup>	Yes (up to 5 lbs.)		Yes
Ireland	38 <sup>A</sup>	25g	235 x 162 x 25	Yes incl. Northern Ireland (& Britain to 25g)		
Belgium	42 <sup>A</sup>	20g	235 x 140 x 5	Yes		Yes
Portugal	42 <sup>A</sup>	20g	235 x 140 x 5	Yes		
Britain	43 <sup>B</sup>	60g		Yes	Soon	Yes
Luxembourg	45 <sup>A</sup>	20g	235 x 162 x 5	Yes		
France	46 <sup>A</sup>	20g		Yes incl. 17 Euro. countries (to 20g)		Yes
Austria	51 <sup>A</sup>	20g	235 x 162 x 5	Yes incl. 49 Euro. countries (to 20g)		
Denmark	54 <sup>B</sup>	20g		Yes		Yes
Sweden Rates include VAT	55 <sup>B</sup>	20g		Yes	Yes	Yes
Norway	56 <sup>B</sup>	20g		Yes		
Germany	56 <sup>A</sup>	20g	235 x 125 x 5	Yes incl. 60 Euro. countries (to 50g)		Yes
Switzerland	58 <sup>B</sup>	100g	250 x 176 x 20	Yes		Yes
Finland Rates include VAT	61 <sup>A</sup>	50g		Yes incl. whole world (to 50g)	Permissible	Yes
Italy	62 <sup>A</sup>	20g	235 x 162 x 5	Yes incl. Europe + Mediterranean	Yes	Yes

### 3. The “affordable prices” principle

#### 3.1. Purpose of the “affordable prices” principle

The importance of the “affordable prices” element of the tariff principles is highlighted in Regulation 6(1)(a), which characterises the universal service thus:

*“Users at all points in the State shall enjoy the right to a universal service involving the permanent provision of a postal service of a specified quality and, subject to Regulation 10(1) [the tariff principles], at affordable prices for all users.”*

The main economic rationale for the principle is concerned with imposing external constraints on prices and on An Post’s costs and efficiencies. Also, the EC Green Paper that gave rise to the 1997 Directive suggested a need to prevent any unnecessary price increases that might result from the introduction of competition in the postal sector if economies of scale were to be lost:

*“protection is needed to ensure that these network ‘fixed’ costs are spread over a sufficiently large number of units that the resulting unit prices are affordable to all.”*

Against this background, the Director considers that the implication of the “affordable prices” principle is that prices should be kept at the lowest possible level, taking account of other legislative constraints and the need for An Post to be able to cover its reasonable costs and finance its activities.

The tests that might be applied to determine if prices are “affordable” are discussed in detail in this section.

<b>Question 3.1</b>	Do you agree with this approach to the “affordable prices” principle, and, if not, please provide details of an alternative approach?
---------------------	---

#### 3.2. A transparent affordability benchmark

The Directive and Regulations provide little guidance on how the “affordable prices” principle might be applied in practice. No clear interpretation has been given in other countries of the word “affordable”, although some countries (such as Germany) require in their legislation that prices should reflect efficient costs.

The Director considers that there would be benefit in establishing a set of transparent criteria against which the affordability of prices can be assessed.

The Director would propose to have regard to these criteria when monitoring An Post's compliance with the tariff principles. She believes that the existence of transparent criteria would enhance the stability and predictability of the regulatory regime.

<b>Question 3.2</b>	Do you agree that the Director should set transparent criteria against which to assess whether An Post's tariffs are affordable? If not, please provide reasons.
---------------------	--

### **3.3. Requirements for an affordability benchmark**

The Director proposes that the following requirements are reflected in her approach to assessing whether prices are "affordable".

The models used for regulating utilities tend to link future prices to past prices. This might be taken as a starting point in the assessment of affordability: in other words past prices may be regarded as affordable. This presumption is reinforced by the fact that prices in Ireland currently compare favourably with those in other countries on a range of measures.

Efficiency also contributes to affordability: prices that reflect efficient production will be more affordable than prices that reflect inefficient production.

Finally, price and quality requirements should be seen as a package, so that the affordable price for a low-quality service would be lower than for a higher-quality service. It should be noted that the benefits of higher quality are potentially reinforced in the case of the postal service by economies of scale: higher quality leads to higher demand, higher volumes and thus relatively lower unit costs.

<b>Question 3.3</b>	Do you agree with the above requirements for the establishment of a transparent affordability benchmark? If not, please give details of proposed alternatives.
---------------------	--

### 3.4. CPI-X as an “affordability” benchmark

If there are substantial economies of scale and/or a reserved area where entry is not allowed, then competition cannot be an effective constraint on prices, at least in the short term. In these circumstances, the test the Director proposes to apply in measuring “affordability” is whether prices are the lowest prices compatible with the continued operation and financial viability of the service provider.<sup>7</sup>

For services for which there is no foreseeable prospect of effective competition, a robust benchmark of affordability could be developed along the lines of the utility regulation models used for infrastructure networks. These are characterised by the following key features:

- the service being regulated is not subject to effective competition;
- the form of price control is medium-term CPI-X (typically set for three to five years); and
- the parameters of the control are set to permit the regulated firm the expectation of recovering efficiently incurred costs and making a return on capital equal to its weighted average cost of capital.

Setting a price cap under this model involves the identification of the *minimum sums necessary to finance the functions of an efficient operator*. The concept of “minimum” is to be taken in the long-term, and the assessment will need to take account of incentives for efficiency, and to incorporate regulatory credibility and certainty so as to encourage the funding of future investments.

Such a model would be consistent with the 1991 EC Green Paper on Postal Services, which clearly assumes that in at least part of the universal postal service there is no effective competition:<sup>8</sup>

*“Universal service causes network costs because of the need to balance out differences in costs*

---

<sup>7</sup> However, some parts of the postal sector, such as sorting, may well be capable of supporting effective competition. An assessment of affordable prices might therefore combine different techniques to determine the contribution of different components of the service to the price.

<sup>8</sup> European Commission (1991) Green Paper on Postal Services, paragraph 3.2 (pages 186-7).

*of providing services in different areas. Such universal networks have significant costs that do not change with volume – particularly for collections and deliveries.*

*In order to ensure the viable continued provision of the universal service network, protection is needed to ensure that these network “fixed” costs are spread over a sufficiently large number of units that the resulting unit prices are affordable to all. This protection can be given in the form of reserved services, granting special and exclusive rights to a service provider or providers.*

*It would be very costly if more than one service provider established parallel networks for standard services.”*

The Director’s proposal is therefore to measure the affordability of services provided by An Post against a transparent CPI-X affordability benchmark, following the model of CPI-X price formulae in utility sectors. The affordability benchmark would also form the basis for future assessments of the affordability of An Post’s universal service tariffs.

The best model would be a multi-year price benchmark. This type of formula can combine the protection of users and the provision of incentives for the regulated firm to make efficiency improvements (including through economies of scale if improvements in service lead to greater volumes of mail).

<b>Question 3.4</b>	Do you agree that An Post’s compliance with its affordability obligations should be assessed by setting a multi-year CPI-X formula? If you believe that some other measure would be preferable, please give details.
---------------------	--

### **3.5. Scope of affordability benchmark**

The Director proposes that effective competition be used as the test for determining the services that should be included within the scope of the affordability benchmark, so that only those universal services on which An Post does not face effective competition would be included within the scope of the affordability assessment.<sup>9</sup>

<sup>9</sup> Applying the affordability test to an average of prices for all universal services would not only be unnecessary: it could give scope for undue cross-subsidisation from the non-competitive sector to competitive services.

The Director considers that affordability would be sufficiently protected by the competitive process for services in which An Post faces effective competition.

A market assessment exercise would therefore be required to determine the boundaries of the sector without effective competition. This would test whether competition is sufficient to protect the affordability of services.

The scope of the benchmark would be reviewed periodically as the benchmark is itself reset.

<b>Question 3.5 a</b>	Do you agree with the use of an effective competition test to assess whether each service should be included within the affordability benchmark basket? If you believe that some other criteria would be preferable, please give details.
-----------------------	---

There might also be benefits in setting “backstop”<sup>10</sup> affordability benchmarks for universal services outside the basket which are contestable or where competition is emerging, for an interim period until competitive pressures are fully effective.

<b>Question 3.5 b</b>	Do you agree that backstop affordability benchmarks should be defined for prospectively competitive services outside the main affordability basket? If so, what types of services should this cover, and why?
-----------------------	---

### **3.6. Structure of tariff basket**

A possible structure for the main tariff basket would measure the change in average price over a given year, taking a weighted average across all relevant services, which should not exceed change in CPI-X. The weights used in working out the average price will be the previous year’s revenue shares. “All items” CPI is the usual deflator, but another measure of inflation could be used if deemed appropriate.

<b>Question 3.6 a</b>	Do you agree with the use of a tariff basket to assess affordability? If you believe that some other form of composite price would be
-----------------------	---

<sup>10</sup> ie upper limits on price increases for particular services or parts thereof.

	preferable, please give details.
<b>Question 3.6 b</b>	Do you agree that “all items” CPI should be the deflator? If you believe some other measure should be used please give reasons.

In addition to the main tariff basket, there might be a need for “backstop” affordability benchmarks for individual prices within the tariff basket (perhaps using a CPI+Y formula, to permit tariff re-balancing within the basket).

<b>Question 3.6 c</b>	Do you agree that backstop CPI+Y affordability benchmarks should be defined for individual services within the main affordability basket?
-----------------------	---

### **3.7. Process for setting affordability benchmark**

If the Director decides to establish a CPI-X affordability benchmark, the following work will need to be progressed by the Office.

A market assessment would be required to identify the services for which competition is not an effective constraint on An Post’s prices and quality of service. Taken together with other considerations, including the extent to which An Post is able to allocate its costs and revenues between different services in a robust manner, this would determine the scope of the main affordability benchmark.

When choosing the “X” for the CPI-X benchmark three elements will need to be addressed:

- an estimate of the scope for An Post to improve its productivity in real terms over the life of the benchmark would be required.
- the projection of volumes, given that greater volume lead to lower unit costs in the presence of economies of scale. Other projections, in particular of future investment requirements, may also be required.

- the costs required by an efficient operator to deliver appropriate levels of service taking into account the universal service obligations of An Post and the expectation of making a return on capital equal to its weighted average cost of capital.

The Director proposes that the starting point for the CPI-X formula will be set when the separated accounts confirm that no unfair cross-subsidy of services in the competitive area exists.

The detailed arrangements in respect of the above would of course be the subject of a future consultation paper.

<b>Question 3.7</b>	Do you agree that the elements outlined above would be necessary to establish a robust CPI-X affordability benchmark?
---------------------	---

## 4. The “geared to costs” principle

The Director considers that the requirement that prices be “geared to costs” should establish a link between the prices charged by An Post and the actual costs reported by An Post’s cost accounting system (as required by Regulation 12 - see Consultation paper “*Universal Postal Services - Accounting Separation & Costing Methodology Proposed Direction to An Post*” ODTR 01/29).

The main economic rationale for the “geared to costs” principle is considered to be to ensure that tariffs are not excessive and to prevent unfair cross subsidies.

For services that are not exposed to competition this implies that the prices charged should bear a close relationship to the cost of providing the service, taking account of the need to subsidise the cost of the universal service obligation, for An Post to be able to finance its activities and other legislative constraints.

For services exposed to competition, unfair cross-subsidisation could be damaging to competition. Another potential concern might be the provision of loss making services to give unfair preference to particular industries or user groups.

In assessing compliance with the “geared to costs” principle the Director proposes an initial assessment of effective prices against average unit cost at the national level for each service. This would involve a three step test for routine examination of tariffs to determine whether particular prices are potentially anti-competitive:

1. Insofar as the price for a service covers the fully allocated cost incurred in providing it, the Director is unlikely to have any concerns about anti-competitive effects.
2. Prices that are found to be lower than average variable costs would be presumed to be not “geared to costs” and potentially anti-competitive.
3. Where a price falls between fully allocated total cost and average variable cost of service provision, an investigation might be required to determine whether or not the price was appropriately geared to cost.

<b>Question 4</b>	Do you agree with the proposed approach to routine examination of whether or not prices are geared to cost? If not, please provide details of your preferred approach.
-------------------	--

## 5. Geographically uniform prices

There is currently no legal obligation on An Post to apply geographically uniform prices, but it seems likely that An Post might wish to retain them for commercial reasons.<sup>11</sup> Additionally it will be noted from the information set out in Table 2.1 that some countries, notably Germany, Finland, France, Austria and Italy, extend the concept of Uniform prices to most (or all) of Europe, in line with an EC Commission recommendation in 1979 that inland tariffs should apply to intra-Community letters at least up to the first weight step.

<sup>11</sup> An Post might in particular value the relative administrative simplicity, and ease of customer information, that are afforded by uniform prices. The net costs of uniform tariffs against which these benefits are set may not be great: in a study for the European Commission, NERA has estimated the cost of the Universal Service Obligations on An Post as 5.4% of turnover on a fully allocated basis, and 0.3% on a net avoidable cost basis. “*Costing And Financing Of Universal Service Obligations In The Postal Sector In The European Union*” Final Report For EC DG XIII November 1998 [Table 5.2]

Taking account of the importance of regional policy for the economic and social well-being of Irish people generally, the Director, as a general principle favours uniform tariffs. The Director proposes to assess compliance with the “geared to costs” principle at a national level, and geographically uniform prices would not therefore conflict with that principle even if costs vary geographically. The Director also has the power, subject to the Minister’s consent, to decide that a uniform tariff shall be applied throughout the state, should An Post submit proposals which involve any change in the status quo.

<b>Question 5</b>	Do you agree that the Director should assess compliance with the “geared to costs” principle at a national level? If you disagree please provide reasons.
-------------------	---

## 6. Individual agreements with customers

The Regulations specifically provide that An Post has the right to conclude individual agreements on prices with customers. Costs vary for different types of users (for example between business and residential deliveries), as well as geographically, and it may be reasonable that this should be reflected in the prices charged where the variations are material. There are two aspects that the Director will examine on a continuing basis.

The Director intends to review on a regular basis whether the framework within which such agreements are negotiated is consistent with the other tariff principles. The Director sees merit in An Post publishing its discount criteria, which should then be applied in a non-discriminatory way - see section 7.

The second aspect is concerned with ensuring that An Post does not unfairly discriminate between customers. This problem might arise, for example, if customers with the same level of business were not offered comparable terms. Potential areas of concern could include volume discounts, as well as any pre-sorting or other discounts that do not relate directly to the costs avoided.

<b>Question 6</b>	<p>Do you agree with the Director’s proposal that An Post should be required to publish its discount offers, eg in relation to volume, pre-sorting, early/late presentation or for any combination of these?</p> <p>Do you consider that other aspects of individual agreements should also be reviewed in this way? Please outline and give reasons.</p>
-------------------	---

## **7. The “transparent and non-discriminatory” principle**

The Regulations require that tariffs be transparent and non-discriminatory. The Director intends to verify compliance with this principle on an ongoing basis. Much of this work will be undertaken as part of the review of An Post’s separated accounts. In particular, non-discrimination between the transfer prices charged between divisions of An Post, its subsidiary or group companies and the prices offered to other operators would need to be confirmed.

<b>Question 7</b>	<p>Do you agree that compliance with the “transparent and non-discriminatory” principle should be monitored as part of the review of An Post’s separated accounts? Please give your reasons if you disagree.</p> <p>Do you consider that this principle should be monitored in respect of other matters/in other ways?</p>
-------------------	--

## 8. Monitoring compliance with the tariff principles

The Director will need to check that pricing policies comply with the tariff principles and are not anti-competitive. Compliance with the tariff principles, especially the “geared to costs” principle, will be tested whenever An Post changes its prices. A full assessment would be made each year in any event, to reflect the operation of the CPI-X formula in benchmarking “affordability”.

The Director believes that the main form of upper limit on prices comes from the “affordable prices” tariff principle. If there are instances in which prices are lower than reported costs, the Director will consider whether this discrepancy is required in order to achieve affordability, and whether this should outweigh the “geared to costs” principle in the particular instance. The Director is mindful of the need to act as a surrogate for competition in encouraging the achievement of efficiency improvements by An Post.

<b>Question 8</b>	Do you agree that the Director should monitor individual price changes to assess whether An Post’s tariffs comply with the tariff principles? Do you agree that when there is conflict between “geared to costs” and “affordability” the Director should take into account An Post’s capacity to improve efficiency?
-------------------	--

## 9. Submitting comments

The consultation period will run from Monday 14<sup>th</sup> May to Friday 15<sup>th</sup> June 2001 during which period the Director welcomes written comments on the issues raised in this paper. Having analysed and considered the comments received, the ODTR will review the interpretation of tariff principles and publish a report on the consultation in July 2001. The ODTR will publish the names of all respondents and may summarise the responses received as part of its report on the consultation.

All comments are welcome, but the task of analysing responses will be simplified if comments are referenced to the relevant question numbers from this document.

In order to promote further openness and transparency, the ODTR will make copies of the comments available for public inspection at its offices, excluding commercially sensitive

information. Where material that is commercially sensitive is included in a response, this should be clearly marked as such and included in an Annex to the response.

All responses pursuant to this consultation should be clearly marked "Reference: Submission re ODTR 01/--" and sent by post, facsimile or e-mail to:

Ms. Jean Bonar

Office of the Director of Telecommunications Regulation

Irish Life Centre

Abbey Street

Dublin 1

Ireland

Phone: + 353 1 804 9600

Fax: + 353 1 804 9665

Email: [bonarj@odtr.ie](mailto:bonarj@odtr.ie)

To arrive on or before 5.00 p.m., on Friday 15<sup>th</sup> June 2001.

Apart from acknowledging responses, the Director regrets that, during the consultation period, her Office will be unable to enter into correspondence with persons contributing comments on this consultation paper.

Office of the Director of Telecommunications Regulation

Monday 14<sup>th</sup> May 2001.

*This consultation paper does not constitute legal, commercial or technical advice. The Director is not bound by it. The consultation is without prejudice to the legal position of the Director or her rights and duties under legislation.*