

Newsletter

The Free and Fair Post Initiative Newsletter
N° 24 – June 2010

Free & Fair Post

EDITORIAL



Philippe Bodson

The Member States have only a few months left to fully implement the Third Postal Directive in their national legislation. At the end of this year postal markets will have to be fully liberalised in most of the Member States.

However, questions remain as regards the universal service guarantee. The Directive foresees that Member States shall ensure that users enjoy the right to a universal service. The definition of the universal service obligations vary from one Member State to another. For instance, some of them include the distribution of periodicals while others do not.

Moreover, the methods of how to finance the universal service obligation and calculate its net costs are also unclear.

This newsletter focuses on this issue. We are therefore happy to have received a contribution from Alex Dieke, from Wik consultancy, who has already prepared several studies for the Commission on postal regulation and the evolution of the postal market, and is currently developing a new study on the external dimension of the EU postal acquis. On the basis of his expertise in the sector, Alex Dieke tried to give a general answer to the following complex question: What is the net cost of the universal service obligation?

The financing of the universal service obligation is directly linked to another question: What is allowed and what should be considered illegal State Aid? We thus decided to further analyse the role that the European Commission plays in this area.

In the current context of postal liberalisation, it is key that the Commission actively plays its regulatory role, as more than ever, its decisions will be analysed and could serve as "jurisprudence" for the future. Anticompetitive behaviour, as well as State Aid, should not be allowed in the newly liberalised postal market.

Philippe Bodson ■

VIEWPOINT

What is the net cost of a universal service obligation?

*By Alex Dieke, Head of Department
'Postal Services and Logistics', WIK, Bad Honnef, Germany*

The traditional view in postal politics has been that the requirement to provide universal service throughout a country is not commercially viable, and that the universal service obligation (USO) is a burden on any operator that is faced with such an obligation. Traditionally, this supposed burden was used as a justification for maintaining postal monopolies ('reserved areas'). However, there is little real-life evidence so far to support that universal postal service cannot be provided profitably and without any subsidy. On the contrary, universal service is provided without any subsidy to finance USO burdens in all countries that have fully liberalised their postal markets so far (Sweden in 1993, Finland 1997, UK 2006, Germany 2008, Netherlands 2009, Estonia 2009).

The Third Postal Directive (2008/6/EC) has formally introduced the term of USO net costs to the postal sector, and has thereby substantially clarified how the potential burdens of universal service should be measured. According to this Directive, universal service providers may be compensated only if 'a Member State determines that the universal service obligations, as provided for in this Directive, entail a net cost [...] and represent an unfair financial burden on the universal service provider(s)'.

It is important to note that calculating 'net costs' is not merely a cost accounting exercise. An annex to Directive 2008/6/EC provides detailed 'guidance on calculating the net cost, if any, of universal service'. This methodology largely follows an economic approach referred to as the 'profitability cost approach' (developed by leading economists Panzar and Crémer et al. in 2000/01). According to this approach, the net cost of the USO is the difference between the profit of a postal operator subject to a USO and the profit of the same operators without this obligation. This net cost can be seen as the drop in profits the operator suffers because of his obligation. Quantifying this cost necessarily requires answering a series of very hypothetical questions: What would the profit of this operator be if it had no USO? What service level would be provided if there was no obligation? How would this change in service affect both sales and costs? At the extreme, the USO net cost is zero if the service that is provided is exactly the same as what the customers demand and pay for. In this case, the regulatory obligation for universal service does not have any effect since operators provide universal service in their commercial interest. If, however, the USO is a binding constraint on a operator, then the net cost could be positive.

The Postal Directive clearly states that net costs must be finally assessed by independent regulators. As a practical matter, calculations are likely to be submitted by providers of universal service that attempt to claim compensation. The task of the regulator is to carefully review this calculation, and correct or alter it where appropriate. Even when a net cost can be quantified, this does not automatically trigger compensation – as the Directive allows to compensate only such net costs that 'represent an unfair financial burden'. The final step of the regulatory process begins when a national regulator has concluded that there is a net cost, and introduces compensation. Like any other public compensation, USO net cost compensations are subject to State Aid control by the European Commission.

Conclusion: The notion of net costs in EU postal legislation provides a sound, yet complex, framework to support public compensations for postal operators where necessary. The procedures for introducing such compensation are likely to effectively limit any excessive subsidies. ■

How to guarantee that postal incumbents do not benefit from State Aid?



The Third Postal Directive foresees the opening of the postal market in most of the Member States by the end of this year. On 1 January 2011,

postal markets should be liberalised in 17 Member States, including 6 Member States that have already opened their markets. The reserved area which is currently used to finance the universal service obligation will then disappear. The question is thus "how will the universal service obligations be financed?" What is authorised and what constitutes unfair State Aid?

According to the European regulation, Member States have two ways to ensure the funding of the universal service obligation net costs:

- Public fund compensation
- Sharing of the net cost of the universal service obligations between providers of postal services or users

In the Member States which have already opened their market, no compensation has been awarded for the USO even if some of them foresee the possibility of spreading the net costs between all postal operators.

As highlighted in the previous article of this newsletter, the decision to compensate USO net costs should be based on the calculation of these net costs. However, large differences remain amongst the Member States in their evaluation of the costs that universal service obligation will induce, especially in the ones which have yet to open their market.

The Commission developed a notice in 1998 on the application of the competition rules to the postal sector and on the assessment of certain State measures relating to postal services some years ago. However, this notice is completely out of date as the rules have changed with the adoption of the Third Postal Directive, which foresees the end of the reserved area by the end of the year. It would therefore be relevant for the Commission to update its rules for assessing whether State financing is compatible with the European competition rules.

In parallel to the progressive liberalisation of the postal market, it is important to ensure that fair competition can develop in this market. The European Commission therefore plays an essential role, as it is currently the only institution which has the regulatory powers to intervene when competition law is infringed.

The European executive has assumed its responsibilities and played a significant role in the past years by taking numerous important decisions in cases dealing with the abuse of dominant position or unfair State Aid. However, several competition cases are still pending awaiting Commission decisions.

In the current context of postal liberalisation, it is key that the Commission is active as regards any competition issues in the postal sector. More than ever, its decisions will be analysed and could serve as "jurisprudence" for the future. Anticompetitive behaviour, as well as State Aid, should not be allowed in the newly liberalised postal market.

Competition decisions have been key in the implementation of the Third Postal Directive and the development of a fair postal market. It is therefore key that the Commission continues to take decisions on current pending cases, such as the case related to the Belgian Post or Deutsche Post. ■

- **15 July 2010:** Mail Forum 2010, Roma
- **6-8 October 2010:** Post-Expo 2010, Copenhagen

