



EUCLID
LAW

The Competition Law Firm

Is mandatory access to the postal network desirable and if so at what terms?

Copenhagen Economics conference

20 June 2017

Prof. Dr. Damien Geradin



AGENDA

- The questions this paper seeks to address are:
 - Whether postal incumbents should be mandated to give access to their network and, if that is the case,
 - At what terms.
- Paper on which this presentation is based is long and detailed. I will only focus on my main findings.
- Key messages are that:
 - Mandatory access is not generally not worth it because it only allows competition at the (very) margin; and
 - If access is not given at the right price, it will be detrimental to the postal incumbent. Access should be based on the retail-minus / ECPR methodology.

MANDATORY ACCESS OR NOT?

CLARIFYING THE CONCEPTS (1)

- Competition that may be created by access to the postal network may come from different entities:
 - Large postal users (or the intermediaries acting on their behalf) may choose to internalize some services situated “upstream” in the postal chain such as collection, pre-sorting, transport, etc. for which they may be more efficient than the incumbent (“work-sharing”). They are compensated through a discount on the price of the stamp based on avoided costs.
 - Alternative postal operators may also decide to use the incumbent’s network in order to provide a “full” postal service to the benefit of their customers in competition with the incumbent. The tasks that these operators perform may not be materially different from those postal users or intermediaries perform. The only difference is that they provide a postal service under their own brand and for their own account.

CLARIFYING THE CONCEPTS (2)

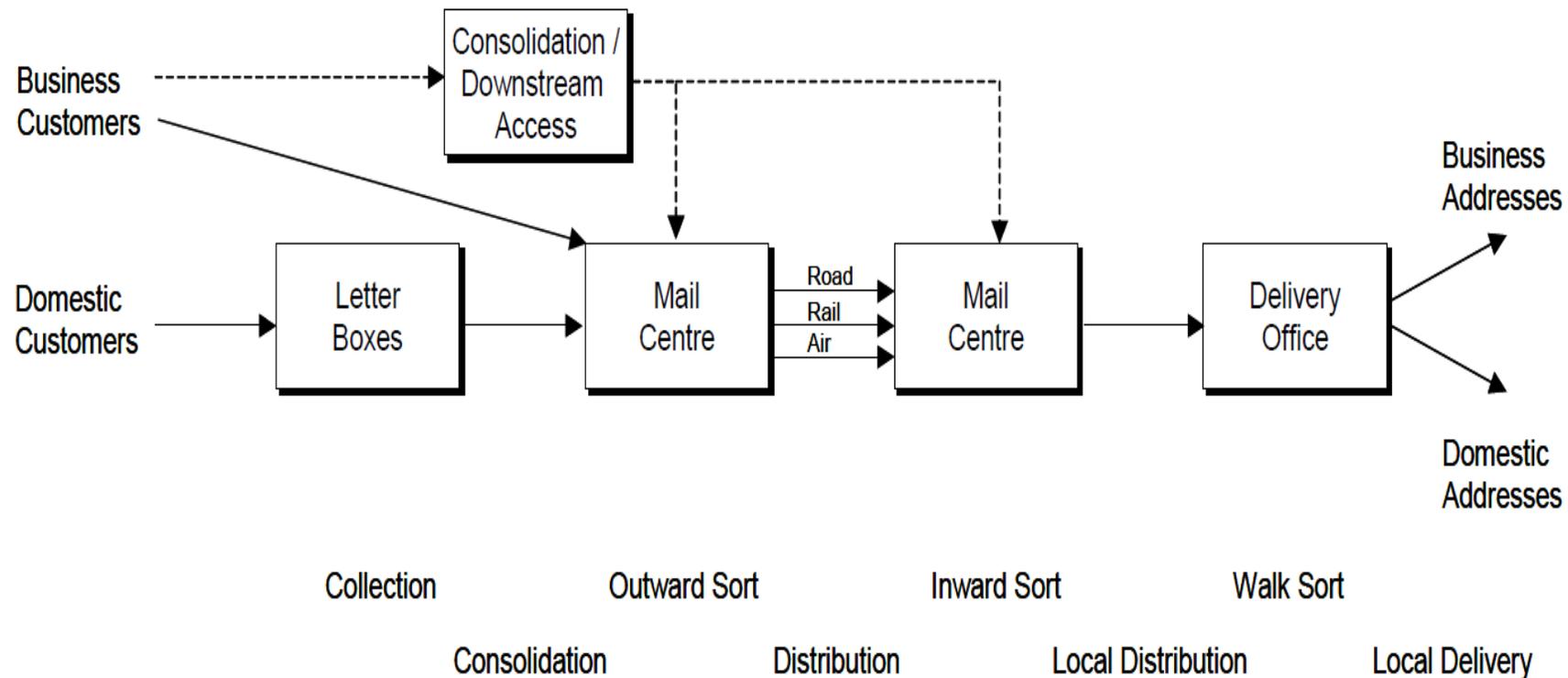
- The incumbent's rivals may engage in three distinct forms of competition:
 - End-to-end competition, whereby the incumbent's rivals exclusively rely on their own infrastructure to provide the service.
 - Access-based competition, whereby they rely on the postal network of the incumbent to perform some parts of the postal transaction, such as for instance sorting, transport and delivery.
 - Mixed competition (also sometimes referred to as mixed by-pass), whereby they engage in end-to-end competition in some parts of the country and rely on the incumbent's infrastructure in others.

CLARIFYING THE CONCEPTS (3)

- It is also important to distinguish between the different possible forms of access to the postal network or infrastructure by reference to the EU postal directive.
- Article 11 of that directive provides that:
“The European Parliament and the Council, acting on a proposal from the Commission ..., shall adopt such harmonisation measures as are necessary to ensure that users and the postal service provider(s) have access to the postal network under conditions which are transparent and non-discriminatory.”
- Article 11bis provides that:
“Whenever necessary to protect the interest of users and/or to promote effective competition, and in the light of national conditions and national legislation, Member States shall ensure that transparent, non-discriminatory access conditions are available to elements of postal infrastructure or services provided within the scope of the universal service, such as postcode system, address database, post office boxes, delivery boxes, information on change of address, re-direction service and return to sender service. This provision shall be without prejudice to the right of Member States to adopt measures to ensure access to the postal network under transparent, proportional and non-discriminatory conditions.”

CLARIFYING THE CONCEPTS (4)

- As to the access to the local network, a distinction can be made between downstream access at the “**outward sorting centres**” and downstream access at the “**inward sorting centres**”.



FEATURES OF THE POSTAL SECTOR AND RELEVANCE TO THE ACCESS TO THE NETWORK DEBATE (1)

- You cannot compare the postal industry with industries relying on physical networks, such as telecommunications or energy.
 - The postal network does not involve any significant sunk costs. The vast majority of the postal network costs are labour costs and other mobile costs, such as for instance vehicles.
 - Postal costs are largely concentrated in the last mile delivery.
 - The demand for postal services tends to be highly concentrated, i.e. a relatively small number of users (large banks, insurance companies, utilities, administrations, etc.) represent a very high share of total demand.
 - The ladder of investment theory does not work in the postal sector.

FEATURES OF THE POSTAL SECTOR AND RELEVANCE TO THE ACCESS TO THE NETWORK DEBATE (2)

- Moreover:
 - While the cost of delivery may vary greatly between low-cost areas (urban areas) and high-cost areas (rural areas), universal service obligations typically mandate the incumbent to provide its services at uniform, geographically-averaged retail prices.
 - Access to the postal network at the level of outward sorting centres is already voluntarily given by postal incumbents via work-sharing agreements.
 - There may be some policy trade-offs between access-based competition and end-to-end competition. The reason is that the promotion of access-based competition tends to have a negative effect on end-to-end competition as the incumbent's rivals may find it preferable to rely on the incumbent's network rather than build their own facilities.

UK EXPERIENCE OF ACCESS TO THE NETWORK IS NOT POSITIVE

- Important lessons can be drawn from the UK's access regime.
 - An access regime that privileges the interests of access seekers to the detriment of the incumbent is bound to fail.
 - The ladder of investment theory does not work in the postal sector. Access did not stimulate significant investments in postal infrastructures.
 - The UK experience confirms that access-based competition is competition at the margin as while access entrants captured close to 50% of mail volumes, they only generated 2% of the sector's revenues.
 - The UK's access regime generated little benefits to small companies and individual users.
 - Developing and implementing an access regime is a regulatory-intensive process.

CONCLUSIONS ON ACCESS

- It is questionable whether mandatory access to the postal network is desirable considering that:
 - Access to the network is already largely given by postal incumbents to their large customers and the intermediaries acting on their behalf, as well as to competitors when they exist;
 - At best, access to the competition network allows competition at the margin.
 - Access is unlikely to deliver any benefit to small users and may on the contrary threaten universal service; and
 - It is likely to impose a heavy burden on the regulator, as well as significant transaction costs on the incumbent.

**AT WHAT RATES SHOULD ACCESS BE
PRICED?**

REGULATED V. UNREGULATED ACCESS PRICES

- A *first* option is to allow the incumbent to set the access price based on the methodology of its choice.
 - This approach does not amount to *laissez faire* since, unless bulk mail is outside the scope of universal service, the access prices in question are subject to the requirements of the postal directive, including the obligations of cost-orientation, and non-discrimination contained in Article 12 of the postal directive.
 - Even when bulk mail is outside the scope of universal service, abusive pricing practices, taking the form of excessive, exclusionary or discriminatory pricing, would breach Article 102 TFEU or equivalent provisions under national competition law.
- A *second* option is for the postal regulator to set the access price. This can be done either directly by setting an access price based on one of the access pricing methodologies or indirectly by adding a minimum margin on top of the retail price.
- A *third* option is to allow the incumbent to set its access prices, subject to an *ex post* control by the regulator.

ACCESS PRICING METHODOLOGIES: COST-BASED MODELS V. ECPR V. BENCHMARKING

- The main approaches are:
 - Cost-based methodologies, either based on historical costs or on long-term average incremental costs (LRAIC).
 - ECPR: Rate is based on retail price minus the costs avoided by the incumbent
 - Benchmarking. Can be a valid methodology depending on what you use as a benchmark.
 - Using REIMS terminal dues is a bad idea:
 - These rates do not necessarily reflect costs (the idea is to improve on the UPU's dysfunctional system).
 - They are based on reciprocity.

OF ALL THE OPTIONS, ECPR IS THE ONE WITH THE MOST ATTRACTIVE FEATURES

- It is in theory simpler to implement for the regulator as it only requires to calculate the costs that are avoided by the incumbent when rivals perform the service up to the selected access points.
- The ECPR model ensures that only efficient entry takes place, i.e. competitors will only enter the market if they are able to provide the competitive segments of the market at a cost that is lower than the cost of the incumbent.
- The incumbent maintains its profits on the mail volumes delivered by the access seeker. Important when the USO is not subject to any State compensation.
- As the wholesale price is linked to the retail price, the incumbent loses the ability to engage in margin squeeze.
- It is supported by leading regulatory economists (Panzar, Armstrong, etc).

CHALLENGES CREATED BY MIXED BY-PASS (1)

- The paper demonstrates the devastating effects on the incumbent of a scenario where it would face rivals operating under a mixed by-pass model, while being obliged to maintain a uniform retail price throughout the territory.
- This leaves the regulator with several options:
 - Rebalance postal tariffs so that retail prices truly reflect the cost of service. This would mean a decrease of the price of mail destined to urban areas and increase the price of mail destined to rural areas.
 - Reduce the scope of the universal service by, for instance, decreasing the number of weekly deliveries in rural areas. Depending on the access pricing model, this may somewhat alleviate the financial losses of the incumbent, but not solve them entirely as cream-skimming would remain.
 - Increase the price of the stamp. While this might once again somewhat alleviate the financial woes of the incumbent, it would be a strange outcome that an effort designed to stimulate competition by granting access to the postal network would generate a retail price increase.
 - Impose on access seekers to hand in mail volumes to the incumbent that reflect a mixed geographical pattern (i.e., the same percentage of low-cost and high-cost mail normally handled by the incumbent), thereby preventing these operators to use the postal network exclusively for delivering mail in high-cost areas.
 - The final option would be for the regulator to adopt a zonal pricing approach, whereby access prices would vary depending on the cost of delivery of the mail volumes delivered by the incumbent.

CHALLENGES CREATED BY MIXED BY-PASS (2)

- The most practical approach would be to charge retail minus (ECPR) access prices to access seekers that hand in mail volumes that reflect a mixed geographical pattern (access-based rivals) and access prices at least as high as the incremental costs for the incumbent to grant access to mixed by-pass rivals.
- This approach would:
 - Encourage efficient entry into the postal segment(s) handled by the incumbent's rivals.
 - Ensure that the incumbent is not forced to subsidize mixed by-pass entrants by delivering their mail in high-cost areas at a price that does not cover the costs it incurs.

Thank you.



The Competition Law Firm

www.euclid-law.eu

Belgium

Euclid Law SPRL
177 Av Louise, Bte 8
1050 Brussels

UK

Euclid Law Ltd.
Berkeley Tower 91, 48 Westferry Circus
Canary Wharf E14 8RP
