

## III-2.6: On May 28, 2010, the ARCEP (French postal and telecommunications regulatory authority) publishes a report it commissioned from WIK Consult, detailing methods for evaluating intangible benefits that accrue to La Poste (the French postal service) from its universal service obligations

Thursday 3 June 2010, by Alex Raiffe, Junior Editor

« Definition, classification and methodology for evaluating intangible benefits related to universal postal service », commissioned by the ARCEP from WIK Consult

### MAIN INFORMATION

On May 28, 2010, the Autorité de régulation des communications électroniques et des postes (ARCEP — French postal and telecommunications regulatory authority) published a report it ordered from WIK Consult, which details the tangible and intangible benefits accruing to La Poste (The French postal service) as a result of its universal service obligation, which are to be included in calculating compensation provided to the universal service provider for its universal service obligations, in application of the European Union's Third Postal Directive liberalizing the postal market in the European Union. This report is critical in tone, but La Poste takes issue with its methodology and conclusions.

### CONTEXT AND SUMMARY

Pursuant to European Union Directive 2008/6/EC (The Third Postal Directive), the current monopoly granted to *La Poste* (the French Postal Service) on delivery of letters weighing less than 50 grams (1,76 ounces), will be abolished by the end of 2010.

Compensation for costs related to *La Poste's* Universal Service Obligations (USO) will be granted by either public funds or a compensation fund financed by contributions of postal operators and/or users of postal services.<sup>[1]</sup>

The compensation shall be equal to the net cost of the USO, taking into account "any *intangible* and market benefits," and only if this cost represents an "unfair financial burden on the universal service provider(s)".<sup>[2]</sup> In order to calculate the compensation, "net cost must evaluate benefits, including **intangible benefits**...for the universal service provider"<sup>[3]</sup>, and subtract the amount of these benefits from the compensation to be provided to the universal service provider for its USO.

Since the European Directive makes reference to *intangible benefits*, the *Autorité de régulation des postes et des communications électroniques* (ARCEP — French Telecommunications and Postal Regulatory Authority) commissioned Wik Consulting to perform an analysis of such benefits from which *La Poste* might benefit, given its status as universal service provider in France.<sup>[4]</sup>

The report produced used the following methodology to identify intangible benefits that might accrue to *La Poste* as universal service provider: it conducted a review of relevant research, and a written survey of 6 European postal operators, followed by a telephone interview.

The report concluded that: "a benefit is classified as 'intangible' when a universal service provider's **performance and cost accounting, and its calculation of the net cost of the universal service obligation, does not (fully) reflect the impact on revenues and cost that result from the existence of this benefit**".<sup>[5]</sup>

Furthermore, a benefit is related to the USO if it is "**caused by the additional level of service...that *La Poste* provides only because of the USO, but would not provide otherwise**", or if it "results from a legal right or privilege that is legally related to the provision of universal service, or justified by the USO".<sup>[6]</sup>

The intangible benefits related to the USO were identified as:

#### 1. Economies of scale/scope

- a. *La Poste* would likely reduce delivery days and close post offices in remote areas with 'high unit cost of delivery', if it were not for the USO.
- b. Therefore, *La Poste* would experience a decline in revenue from less items posted, and would lose economies of scale/scope that result from the highest possible volume of mail sorted and delivered.
- c. However, the authors of the report believe that *La Poste's* accounting methods and performance indicators are currently incapable of reflecting changes that would occur without the USO.

#### 2. Enhancement of corporate reputation and brand value

- a. *La Poste* is ubiquitous, enjoys a high-level of customer satisfaction and benefits from a positive reputation as a good corporate citizen. As an aspect of France's cherished *service public*, *La Poste* is perceived positively by the population.
- b. Reductions that would occur in the absence of USO would probably lead to a decline in *La Poste's* reputation, and would affect sales of both USO and non-USO products.
- c. Again, the authors of the report believe that *La Poste's* performance and accounting methods are not capable of estimating the impact of a reduced service level and possibly bad publicity on demand for postal and other services, which constitutes an intangible benefit.

#### 3. Enhanced advertising effect

- a. This is due to *La Poste's* nationwide presence and visibility via post offices, letterboxes, and postal vehicles and workers that deliver mail 6 days a week.
- b. Without the USO, *La Poste* would probably reduce post offices, so it would be less visible.
- c. The authors believe that *La Poste's* accounting and performance accounts do not take this factor into account, making it an intangible benefit.

#### 4. Better bargaining position

- a. *La Poste* is fully owned by the State, which leads to close relationships to local and national politicians. *La Poste* is also one of France's largest employers, with more than half of employees still under the status of civil servant, and most of them unionized. *La Poste* therefore has an advantageous lobbying position.
- b. This benefit cannot be accounted for using accounting principles, and is therefore an intangible benefit. However, only part of this is related to the USO, the other part is due to the fact that *La Poste* is owned by the state, and that it is a large enterprise.

#### 5. Privileged access to the philately market

- a. *La Poste* is the sole authorized printer of French postal stamps, using the Universal Postal Union's standard country mark of 'France'. Such stamps are the only 'true' postal stamps recognized by stamp collectors.
- b. Without the USO, *La Poste* would not be authorized to issue official postage stamps, which would result in less demand by philatelists.
- c. This is an intangible benefit, not accounted for in *La Poste's* accounting.

## 6. VAT Exemption

- a. *La Poste* is exempt from France's Value Added Tax (VAT) tax, whose standard rate is 19.6%.
- b. This gives *La Poste* a competitive advantage with customers that are not allowed to deduct VAT from their purchases, such as private customers, the public sector, and banking and insurance services (because such companies are also exempt from VAT).
- c. However, companies (such as *La Poste*) that are exempted from VAT pay an extra tax on wages, which partially offsets this benefit. About 86% of *La Poste's* income is VAT-exempt.
- d. The analysis of the extent of this benefit includes calculating the amount of *La Poste's* income subject to VAT; the share of postal revenue from VAT-exempt clients; effects resulting from gross price increases; and the extent to which *La Poste* can carry VAT over to its customers.
- e. In any case, the authors believe that *La Poste's* performance and cost accounts do not provide sufficient information to calculate the effect of VAT exemption.

## 7. Exemptions from customs and excise regulations

- a. Article L6-1 of the *Code des Postes et des communications électroniques* (French Postal and Telecommunications Code) provides *La Poste* with a simplified and free procedure for submitting international-bound parcels and packages to customs inspection, as specified by Universal Postal Union regulations and treaties.
- b. Other postal operators do not benefit from this simplified procedure.
- c. *La Poste's* performance and accounting methods do not account for this benefit, which makes it intangible.

## 8. Exemption from transport license

- a. *La Poste*, according to Article 17§8 of French Decree n° 99-752, *La Poste* is legally exempt from transport licenses, whereby transport companies have to deposit a sum of money with the government (minimum 900 Euros per vehicle) to obtain a transport license. These sums are therefore unavailable for equity and debt requirements, and the corporations require extra capital to meet their current and investment expenses. *La Poste* being exempt from this requirement, it benefits from a competitive advantage.
- b. This competitive advantage is not accounted for in *La Poste's* performance and cost accounts.

The report also includes an analysis of **tangible benefits** related to the USO. Tangible benefits are included in *La Poste's* cost and performance analysis, and can be directly related to *La Poste's* status as universal service provider.

Such tangible benefits are:

### 1. Demand complementarities

- a. *La Poste* has 2.7 post offices per 10,000 inhabitants, which provide, besides postal services, sale of stationery and financial services through *La Banque Postale* (The Postal Bank). Without the USO, *La Poste* would probably reduce the number of post offices, and would therefore lose revenue from other services it provides.
- b. Such benefits are apparent from *La Poste's* accounting<sup>[7]</sup>, and will therefore be automatically considered in estimating the net cost calculation the ARCEP will receive.

### 2. Press subsidies

- a. According to subsection B of section 2 of Article R1 of French Decree n°2007-29 of January 5 2007 relating to *Service universel postal et aux droits et obligations de La Poste...* [Universal postal service and the rights and obligations of *La Poste*], the delivery of newspapers and periodicals is included in the universal service obligation. Articles L.4 and R.1-1-17 of the *Code des postes et des communications électroniques* [French Postal and Telecommunications Code] oblige *La Poste* to promote diversity of the printed press.

In order to achieve this goal, *La Poste* is granted a financial compensation determined by a tripartite agreement signed by *La Poste*, the French State, and publishers' representatives.<sup>[8]</sup> According to this agreement, *La Poste* receives 242 million Euros per year, which is supposed to be gradually reduced to the sum of 180 million Euros by 2015.

If *La Poste* were to reduce delivery frequency, it would probably violate the aforementioned decree and provisions of the *Code des postes*, which would result in the loss of this subsidy.

- b. This benefit is tangible, because it is included in *La Poste's* accounting.

Finally, the report takes into account **other commercial benefits** that are not related to the USO, but relate to *La Poste's* unique historical and cultural position as sole postal operator in France for centuries. Such advantages would exist even without the USO, and are included in the report in order to help the ARCEP assess their impact on *La Poste's* market position and costs. Such benefits are not mentioned specifically in the European directive, but could eventually be used by the ARCEP in asymmetrical regulation, and include:

1. **La Poste's market-dominant position:** *La Poste* dominates the French postal market, since competition for letters has not yet emerged. According to the report, even in countries where the postal market has been opened to competition, the historical operator remains dominant. This is because of consumer inertia (the price of a stamp is not significant enough for households to seek out competitors), and the fact that the actual cost of sorting and delivering letters is higher than the price of the stamp. Therefore, competition is only truly effective for large-volume senders, who can benefit from significant savings by using competition to their advantage. However, this advantage is not related to the USO, because without it *La Poste* would have more freedom in setting prices and in protecting its market share; nonetheless, it is doubtlessly a circumstance to *La Poste's* advantage.

2. **Strategic advantages in prices and acquisition:** *La Poste's* size might allow it to acquire competitors (it has already acquired a number of foreign parcel carriers). *La Poste's* volume of delivery (280 letters per capita per annum according to the report) allows it to provide lower prices through better economies of scale and a larger offer of services than its competitors. However, this is not related to the USO, but rather to *La Poste's* structural factors such as its size and historical monopoly.

3. **Detailed knowledge of the market:** Since *La Poste* has never had any competitors, it naturally has the best knowledge of the market, and because of its monopoly, it already has a relationship with all potential customers on the market. This is a factor that would exist with or without the USO.

4. **Interest profit due to prepaid postage:** *La Poste*, just as all traditional postal services, sells stamps in advance of letters actually being sent. This allows *La Poste* to be less dependent on third parties for credit, or to benefit from investment income in the form of interest. Even though all competitors could apply the same system of prepaid postage, *La Poste's* natural size means that it will probably benefit from a more powerful position (more stamps sold) than its competitors.

5. **Ownership of post office boxes:** *La Poste* owns post office boxes and manages the *Cedex*<sup>[9]</sup> system. Delivering mail to post office boxes is less costly than direct delivery, because there is less transport necessary. This allows *La Poste* to save money compared to competitors, and possibly to create complementary demand, by selling other goods and services to customers who come to the post office to pick up their mail. It is improbable that a competitor would develop a parallel system, because of the investment needed, and the unattractiveness for consumers of having multiple post office boxes. Even though post office box service is not part of the USO, it is a pre-existing factor that benefits *La Poste*.

6. **Postal code system:** *La Poste* created and manages the French postal code system to conform to its own, internal logistical structure for mail flow and delivery. Furthermore, since the system has existed since the 1970's, consumers are familiar with it. This means that competitors will have to use *La Poste's* postcode system, even if it does not comply with their internal logistical structure. This gives *La Poste* a competitive advantage, and could create extra costs for competitors. This is not related to the USO, but rather, to the historical monopoly.

7. **Free parking permits:** French towns allow *La Poste's* vehicles to use public street parking for free. However, they do not grant the same privilege to other parcel delivery companies, who have to look for an appropriate parking space and pay the parking fee, or else, face a parking fine. If this situation does not change, it will represent a competitive advantage for *La Poste*. The report makes the suggestion that even if *La Poste* were to lose its parking privileges, agents would probably fine *La Poste* vehicles less often than other vehicles, out of habit.

**8. Tax deductions:** In addition to its USO, *La Poste* is legally required to contribute to national and regional development programs to benefit underdeveloped areas of France. It therefore receives a tax deduction on local taxes on land and buildings to compensate it for maintaining postal presence in rural areas. The amount of this deduction is currently equal to 140 million Euros per year. This is not related to the USO, even though *La Poste* would likely lose this deduction if it were not designated universal service provider.

**9. Privileged access to terminal dues paid by foreign postal operators:** Terminal dues are the system by which postal operators compensate their counterparts in a foreign country for delivering mail they send to that country. These dues are defined by the Universal Postal Union's Convention on Postal Dues<sup>[10]</sup>, and the REIMS convention between European Union postal operators<sup>[11]</sup>. Even though access to UPU negotiations and system is closed to other postal operators, *La Poste's* competitors should theoretically be allowed to negotiate and participate in the REIMS convention. Therefore, despite *La Poste's* advantage in negotiations due to its size, volume, and status of universal service provider, this advantage is not *directly* linked to the USO.

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[1] Editor's note: Cf. *Regulatory Law Review*, 2010, II-2.1

[2] Directive 2008/6/EC Annex 1, Part B, and Article 7

[3] *Idem*, Annex 1, Part B.

[4] ARCEP, *Definition, classification, and methodology for evaluating intangible benefits related to universal postal service*, commissioned from WIK Consult, published May 28, 2010, available at [www.arcep.fr](http://www.arcep.fr) in both French and English.

[5] ARCEP, p.23

[6] *Idem*, pp. 23-24

[7] Cf. European Commission State Aid Decision n°531/2005 on the creation of *La banque postale* (The Postal Bank), for an example of *La Poste's* model for estimating the impact on demand in case of closures of postal outlets.

[8] *Accord tripartite 2009-2015*

[9] *Courrier d'entreprise à distribution exceptionnelle* [Special delivery business mail], a system of special delivery to businesses that receive large volumes of mail: the system works by attributing a special postal code to each 'Cedex' business, which then receives its mail through a special delivery channel, rather than via general delivery to households and smaller businesses.

[10] 2010-2013 dues Schedule available on the Universal Postal Union's website : <http://www.upu.int/en/activities/te...>

[11] Available at : <http://eur-lex.europa.eu/LexUriServ...>

## BRIEF COMMENTARY

Although this report was ostensibly commissioned by the ARCEP in order to establish a methodology via which to fulfill its European Union obligation of determining the amount of subsidy to be provided to *La Poste*, which should be equal to the extra cost incurred by *La Poste* in the fulfillment of its USO duties minus the tangible and intangible benefits that accrue to *La Poste* due to its USO duties.

The report's inclusion of other benefits, besides tangible and intangible benefits, makes one think that the ARCEP is evaluating, via this report, the methods by which it could apply asymmetrical regulation to *La Poste*, just as it did for France Telecom at the end of its monopoly over landline telephone services, in order to promote competition through policies detrimental to the historical monopoly and favorable to new competitors.

However, it is important to note that this study is not an official document, and is simply a study ordered by the ARCEP from a private consulting firm.

*La Poste* itself has made a number of comments on this article, which are available at [http://www.arcep.fr/uploads/tx\\_gspublication/commentaire-laposte-etudeWik-mai2010.pdf](http://www.arcep.fr/uploads/tx_gspublication/commentaire-laposte-etudeWik-mai2010.pdf), and which challenge many of the report's affirmations on the grounds that they are improperly conceived and/or lack objectivity. Some examples cited by *La Poste* are the VAT exemption (which it claims is unfavorable because of the salary tax it owes in counterpart), the system of post office boxes (which it claims is not an advantage, because it is legally required to grant competitors access to the boxes), the claim that *La Poste's* vehicles park for free and are not fined for parking infractions (*La Poste* claims that this is untrue), and the financial advantage that is attributed to *La Poste* based on the fact that it sells stamps before delivering mail (*La Poste* indicates that it only derives an infinitesimal portion of its revenue from prepaid stamp sales, and the bulk of its revenue comes from corporate franking machines, which are post-paid, the enterprise receiving a bill at the end of the month according to the number of letters franked by its machine).

In any case, this document is interesting because it provides, for better or for worse, a framework for understanding the factors that will have to be taken into account in liberalizing the French postal market, including many factors that advantage or disadvantage *La Poste* based on its historical presence and its national size. Let us not forget that *La Poste* has only existed as an independent entity since 1991, prior to which it was part of the Postes, télégraphes & téléphones (PTT — Posts, telegraphs, and telephones) a public, cabinet-level organization. More recently, *La Poste* was transformed from a state-owned company, to a private limited company, whose capital is entirely owned by the State, by Act of Parliament of February 9, 2010 (Cf. *Regulatory Law Review*, 2010 II-2.1). Therefore, it is impossible to affirm that the postal sector is becoming a normal sector that could be governed by general competition law rules, rather than sector-specific regulation: the English and North American examples demonstrate that national postal services must financially bear their public service obligations, which they are unable to do in the long term without receiving significant amounts of public funding. However, this means that this system of legitimate public subsidies must be studied, measured, debated, and we cannot simply accept at face value legislation that uses sovereign power to transfer public monies to a postal operator; it is necessary to demonstrate that such transfers are adequate and proportional: this is the paradigm of Regulation in action.