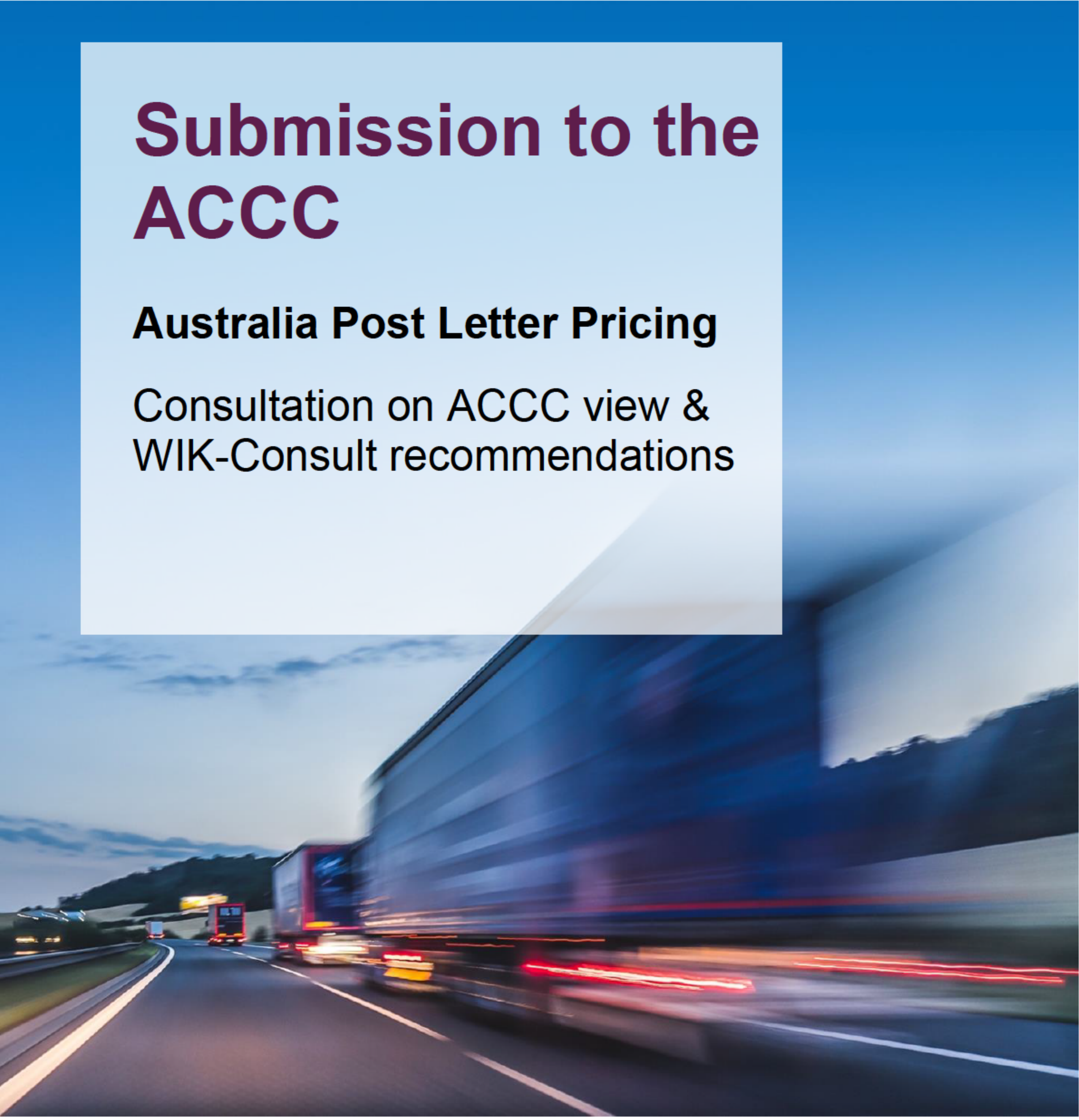

Submission to the ACCC

Australia Post Letter Pricing

Consultation on ACCC view & WIK-Consult recommendations

aramex formerly fastway couriers

FedEx

sendle

TEAM GLOBAL EXPRESS

Supported by

National Retail Association

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Introduction

The signatories to this submission acknowledge the ACCC's preliminary view on the draft price notification is to not object to the 25% reserved letters price increase proposed by Australia Post.

We recognise the importance of Australia Post's Letters infrastructure in providing services to Australians, along with the need for a strong and financially sustainable Australia Post. However, to deliver pricing, policy, and regulatory outcomes to achieve that objective, the right issues need to be addressed.

We are pleased to note that both the ACCC and WIK-Consult have independently identified several critical issues relating to Australia Post's Letters business, which are directly hampering healthy competition in the Australian parcels market and should be urgently addressed.

As outlined in previous public and confidential submissions by signatories to this submission, **the market for eCommerce parcel delivery to residential consumers is approaching a crossroads**, presenting all stakeholders with a choice of what type of parcel delivery market they would like to see in future.

Growth in demand for parcel services to rural & regional Australia is outpacing metro areas, despite services currently being slower and more expensive. A lack of parcels competition is holding back investment in the development of eCommerce trade into and out of rural & regional Australia.

Slow delivery services are restricting the ability of regional businesses to compete. Their dependence on Australia Post means they have no choice in how they supply to their customers, leaving them with higher prices and slower delivery times whilst constraining consumers' access to goods, which in turn adds to regional disadvantage and cost-of-living pressures.

Delivery of residential parcels in Australia is currently dominated by one provider, especially in rural and regional Australia. In these regions, Australia Post has ~95%+ market share based on its control of monopoly Letters last mile infrastructure to support and subsidise parcel deliveries.

Whilst several other parcels providers have the capabilities to carry parcels into rural and regional areas from major cities, low parcel volumes in each individual town and region make it **cost-prohibitive for other parcels businesses to invest in duplicating the local 'last mile' infrastructure needed to compete with Australia Post**.

Australia Post's own commercial parcels businesses, including both **Australia Post and StarTrack branded products, benefit from exclusive access to Australia's Letters last mile infrastructure**, including post offices operated by Licensees.

Australia Post maintains a position of blocking other parcels providers from lodging parcels into the local Letters last mile infrastructure in rural and regional Australia. Instead, it insists that other parcels providers must purchase **bundled end-to-end parcel services, from pickup in originating cities all the way through to last mile delivery**, whether that be to the home or a local delivery point (e.g. Post Office or other pick-up location specified by customers), irrespective of whether parcel providers want or need those upstream services (eg 'first mile' collection and 'middle mile' processing and transportation).

The 'bundling' strategy adopted by Australia Post has the effect of preventing upstream competition, reducing all competing services to the same 'lowest common denominator' of Australia Post's underlying service and forcing pricing based on adding 'margin on margin' – an outcome that is uncompetitive and not commercially viable.

The consequence of this model is:

- **A focus by Australia Post on maintaining and enforcing a bundled end-to-end wholesale service for commercial customers and other carriers,** rather than focusing on optimising and offering the individual components that make up the bundled service.

- **Cross-subsidisation** between Australia Post's Letters and Parcels businesses. For example:
    - Streaming Australia Post and StarTrack-branded parcels to Posties for residential delivery.
    - Parcel collection at Post Offices (both Australlia Post and StarTrack).
    - Sharing of middle mile assets between Letters and Parcels, including StarTrack (including linehaul vehicles, aircraft, processing facilities, metro transport services)

- **Australia Post effectively maintaining an unregulated parcels monopoly in rural and regional areas** by blocking other parcel carriers from accessing Independent Community Post Offices and/or Posties.

While at face value these appear to be issues specific to Parcels, the inappropriate allocation of costs between Australia Post's Reserved and Non-Reserved services, especially when combined with its role as price-setter based on its ~75% market share, is having a profound impact on pricing and fair competition in the Australian parcels market.

The signatories to this submission are concerned about several important issues constraining fair competition in the Australian parcels market based on:

1. **Unfair and inaccurate cost allocations** between reserved and non-reserved services, including parcels and non-reserved 'letters' services (incl marketing leaflets and international inbound packets)
2. **Unfair pricing practices, fundamentally reliant on cross-subsidisation** – between its own Letters and Parcels business, and between regional and metropolitan parcel senders
3. **Insistence on only providing smaller parcels carriers with commercial access to any of its parcel network via forced-bundling**, preventing other carriers from offering genuine competition, alternative providers, faster services, and service innovation, especially for Australians living in rural and regional areas and the retailers who want to sell products to them.
4. **Blocking Independent Licensed Post Offices from being able to provide services to smaller parcel carriers in their local community** (eg collection points, returns lodgment), enforcing unreasonable exclusivity obligations in order to restrict competition, maintaining an effective parcels monopoly in rural and regional Australia.

Furthermore, the proposed letters price increase does nothing to support the ongoing viability of Independent Community Licensed Post Offices. With only ~3% of letters being sent via Post Offices, the proposed price increase represents an average increase in income for Licensees of approximately $6 per week. The history of letter price increases show that each time a significant price increase occurs, volume decline accelerates further. The expected volume decline from the proposed price increase would further reduce that $6 per week of additional income, to as low as $3.

As has been noted in the ACCC and WIK-Consult's respective reports, substantial issues exist in how Australia Post is currently cross-subsidising its Parcels business through its Letters business, and in particular the costs allocated to Reserved Letters.

In the following section, we provide comments, conclusions and recommendations on the issues raised by the ACCC and WIK-Consult assessments of Australia Post's proposal to increase pricing.

ACCC and WIK-Consult's findings and implications for Parcels competition

Page	Issue identified by the ACCC / WIK-Consult	Implications for parcels competition

P4	*We note the information Australia Post has presented in support of its draft price notification has* ***raised concerns about revenue allocation****. In particular,* ***stakeholders identified potential inconsistencies in the way costs and revenue are allocated by Australia Post. We recognise these concerns have the potential to give rise to broader competition impacts and recommend that Australia Post review its revenue allocation processes.***
	
	The ACCC considers that both cost and revenue allocation are important ***because of the competition issues that could arise if Australia Post used the revenue generated from its monopoly letter services to subsidise the parts of its business that operate in competitive markets****. The ACCC will continue to monitor developments in this area, including the appropriateness of Australia Post's allocation of costs and revenue across the reserved and non-reserved services.*
	
	The ACCC is recommending that Australia Post make improvements to the way it models, allocates and recovers costs.
		Desired Outcome: *An independent review of* ***cross-subsidisation of Australia Post's Parcels business by its Letters business*** *be conducted by the ACCC in order to ascertain (1) the extent of cross-subsidisation, (2) identify actions to remove cross-subsidisation, and (3) identify the appropriate level of ongoing regulatory oversight in order to ensure fair competition in the Australian parcels market.*
		
		• Australia Post currently holds ~75% market share in the Australian parcels market.
		• Australia Post's cost allocations between Reserved letters, Non-reserved letters (including unaddressed mail), and parcels have direct implications for Australia Post's price-setting behaviour in the competitive parcels market.
		• Publicly available evidence, including the 2023 Annual Report, strongly suggests that costs are being allocated inappropriately, with:
		  ◦ Costs for parcels and Non-reserved services being allocated to Reserved services, leading to an over-statement of Letters losses
		  ◦ Costs of carrying Non-Reserved Letters (e.g. marketing leaflets and international inbound packets) being conflated with Reserved letters when making assertions about "Letters losses", then using these combined 'Letters' losses to argue for letters price increases and Modernisation reforms, and;
		  ◦ the Parcels business enjoying substantial cross-subsidisation by the Letters business resulting from its free/under-priced and exclusive access to Letters infrastructure and workforce across the first mile (pickups and Post Offices), middle mile (transport and processing) and last mile (posties, Post Offices, parcel lockers).
		  ◦ It appears likely that unusually large losses in the Non-Reserved letters products account for a substantial proportion of Australia Post's total "Letters" losses, and subsequent Enterprise losses.

P4	*We also recognise the critical importance of cost allocation as* ***Australia Post's business changes from focusing primarily on letters to parcel delivery.*** *This is relevant because the proposed price increase*	***Desired Outcome:*** *An independent review of the* ***mechanics of changing fixed cost allocations over time*** *resulting from the substantial and ongoing shift in the balance of letters and parcels carried. The review can consider fixed cost allocations in both the delivery networks and the Post Office networks, with one*

	for the reserved letter services should be commensurate with the costs associated with those services only, and should not be used to cross-subsidise other services that are provided by Australia Post in competitive markets. We have set out some recommendations for Australia Post to improve its cost allocation model to more accurately separate the costs attributable to its reserved and non-reserved services.	*outcome of such a review being the development of a approved formula to ensure fixed costs are appropriately reallocated to parcels services from letters services, over time, to reflect this changing mix.*
		• As identified by Australia Post in its case for Modernisation, the mix of revenue generated by the Letters and Parcels businesses is in a constant state of change, with a substantial ongoing shift towards parcels.
		• This carries significant implications for the ongoing allocation of costs, particularly fixed costs.
		• This ongoing change in mix acts to further compound the issues raised in the previous point relating to cost allocation between Reserved and Non-Reserved services/products.
		• These issues include:
		  • Posties, where evidence suggests that the true cost to deliver a parcel is not being fully allocated to the Parcels business, and is therefore being subsidised by the Letters business
		  • Post offices, where the ACCC and WIK-Consult identified that Australia Post's parcels businesses currently enjoy a 'free ride', with the Letters business carrying the full cost of subsidies to Community Licensed Post Offices, despite ongoing growth in parcel volumes handled by Post Offices.

	We further raise in this report and our recommendations a number of other issues with Australia Post's cost allocation model. These include ***issues with Australia Post's transfer price arrangements with StarTrack****, the basis on which* ***subsidies paid to local Post Offices are allocated*** *within the model, and the* ***absence of short-run and long-run incremental costs within the model****, the latter of which are* ***critical for effective regulatory decision making****.*	***Desired outcomes:*** 1. *An independent review be conducted to assess and approve new rules (and any ongoing amendments) to Australia Post's transfer pricing mechanisms, ensuring the true cost-to-serve is reflected in the prices charged for different Australia Post and StarTrack-branded products.* 2. *The review could evaluate existing international models demonstrating effective approaches to achieving these outcomes. For example, the US Postal Service (USPS) regulated "Workshare" arrangements, where not only the true cost to serve of each step in the delivery is published, but other parcels businesses are able to inject parcels along the delivery chain, paying the same regulated price while contributing to the financial sustainability of USPS's national network.* 3. *New transfer pricing arrangements be published to ensure transparency while providing avenues for appeal and review.* 4. *The new transfer pricing arrangements be designed to facilitate opening of equivalent access to all parcel carriers at a fair, transparent, and regulated price that reflects Australia Post's true-cost-to-serve.* • The ACCC and WIK-Consult have both identified the issues with transfer price arrangements with StarTrack. We strongly agree with this observation, and note that this issue carries significant

implications for parcels competition in the Australian market.

- **<u>However</u>**, we draw to the ACCC's attention that this issue is more concerning in its relevance to Australia Post's "red" parcels products, such as Parcel Post, eParcel and Express Post products.
- These "red", Australia Post-branded products receive even greater subsidisation due to the larger volumes involved. Any current transfer pricing arrangements for these products are opaque and would be susceptible to misallocation of costs.
- Australia Post has openly engaged in a process of reconfiguring its various parcels networks (including StarTrack) to "stream" products between them up and down the delivery chain. For example:
  - Streaming both StarTrack and Australia Post parcel products to Posties for delivery to homes
  - A higher proportion of Postie workload being driven by the house-by-house delivery of Unaddressed Mail (i.e. marketing leaflets), weighing on Postie productivity.
  - Streaming Express Post and StarTrack Premium parcels to each other's networks
  - Installing parcel sorting machines within letters facilities, including those capable of sorting StarTrack parcels
  - Sorting StarTrack parcels in Express Post facilities
  - Collecting letters, Australia Post parcels, and StarTrack parcels using single Australia Post pickup vehicles (eg red vans)
  - Using Post Offices as collection points for letters, Australia Post-branded parcels, and StarTrack-branded parcels.
- Streaming, and the broader interoperability of Australia Post's networks, has allowed various parcel products and brands to be considered independently of the infrastructure used to carry any given parcel. As a result, the "Australia Post" or "StarTrack" branding of any given parcel is no longer an accurate proxy for the network infrastructure, and associated costs, used to carry and deliver those parcels.
- We strongly support these initiatives and the concept of "streaming". They allow Australia Post to best use its existing assets and redeploy infrastructure from the declining Letters business to the growing Parcels business.
- **<u>However,</u>** allocation of costs must follow the reconfiguration, transparently showing benefits in the financial performance of the Letters business, while fairly and appropriately allocating the relevant costs (fixed and variable) to the competitive Australia Post parcels business, including products bearing the StarTrack brand.

		• Australia Post's own commercial parcels products, operating in a competitive market, should not be exempt from such an arrangement, particularly given the much larger implications for parcels competition attached to those products.
	We acknowledge that this assessment has been particularly complex because the outcomes of the postal services modernisation review were uncertain when Australia Post submitted its draft price notification(s). However, the ACCC considers that improved information and processes will be increasingly important if Australia Post moves towards a long-term price path approach in the future, and the cost-based assessment becomes more finely balanced as operating costs are reduced following the implementation of modernisation reforms.	***Desired Outcome:*** *We urge the ACCC to consider deferring its decision to Not Object to the proposed pricing increase until it has been able to assess operating costs following the implementation of the Modernisation initiatives approved by the Government.* • We fully appreciate that without transparency of cost efficiencies released through the Modernisation changes, it would be nearly impossible for the ACCC to fully assess the future operating costs of Australia Post, despite this being essential to any full and proper assessment of pricing increases.
	*We note that in the **absence of improvements to the information provided by Australia Post** in support of any future price notifications, **the ACCC may not be in a position to not object to future proposed price increase.***	***Desired Outcome:*** *We propose that the ACCC defer its decision to Not Object to the proposed pricing increase until it has received adequately improved information from Australia Post, including information that allows it to properly assess and critique current cost allocations and cross-subsidisations.* • A proper assessment of Australia Post's costs and pricing requires full disclosure of information. • We are concerned that the ACCC has being asked to evaluate a pricing increase that, as this statement implies, has been assessed without adequate information, to the extent that the ACCC's is flagging that it may object to future increases should the information provided not be improved. • As outlined in this submission, assessment of Australia Post's costs carries serious implications for parcels competition in Australia. Letters pricing approvals cannot be considered in isolation from the way Australia Post costs and prices its parcels business • Given the provision of inadequate information (quantity and/or quality) by Australia Post to support ACCC's assessment, it is unclear how the ACCC is in a position to not object to the proposed price increase.
	*The ACCC also notes that Australia Post's costs and other financial reporting are not disaggregated by geographic region. In recognising the importance of postal services for regional and remote Australia, **the ACCC recommends that such a disaggregation of Australia Post's reporting between urban and rural areas would be beneficial** – both for the assessment of Australia Post's provision of its community service obligations under section 27(4)(a) of*	***Desired Outcome:*** *Disaggregation of cost accounting and reporting by Australia Post to the ACCC is essential to facilitating a proper assessment of cost allocations. This is even more important as they relate to rural and regional areas.* • The costs to provide letters and parcels services to rural and regional Australia are markedly different. • The identified issues of unfair cost allocation between Reserved and Non-reserved services are compounded in rural and regional areas.

	the Postal Act, and for government policy setting into the future.	• In the geographic areas where Australia Post typically dominates the parcels market (and is often the only player), we would expect the cross-subsidies to be at their greatest. For example, where an Independent Community Licensed Post Office facilitates the collection of a parcel, or a Postie delivers a parcel to a home in a smaller regional town.
P61	*…that Australia Post undertake further work to address the issues raised by WIK Consult, such as:* ***providing short-run and long-run incremental costs of individual services and products, including loss-making reserved services***	***Desired Outcome:*** *The re-instatement of the ACCC's independent annual review of cost allocations, including the ongoing recalculation of incremental costs associated with the provision of a range of services (eg letter delivery, parcel delivery) by a single operational network.* • A thorough understanding of the short-run and long-run **incremental costs** for Australia Post to carry and deliver a letter or a parcel are essential, not only to assess whether those costs are being appropriately allocated, but to assess the remaining costs allocated as "non-incremental" (or notionally fixed costs), and therefore whether cost allocations are fair and appropriate. • We observe that as the postal mix changes over time (with letters declining, parcels growing), the incremental costs of each service change would continue to change dramatically. Without constant evaluation, review and transparency of the mechanism for determining those incremental costs, it is more likely than not that those incremental costs would not remain accurate. • The ACCC ceased its annual review of cross-subsidisation at Australia Post in 2015. At the time, the ACCC determined that cross-subsidisation was not observed. Developments in the market, reconfiguration of Australia Post's network operations (including partial integration of the StarTrack network), and the subsequent cost allocations, mean that the basis for ceasing the previous annual review regime no longer applies.
	…that Australia Post undertake further work to address the issues raised by WIK Consult, such as: ***separately identifying restructuring costs as unattributable costs***	***Desired Outcome:*** *The ACCC (or its consultants/other auditors) conduct an independent and detailed financial audit of the extent to which corporate and/or parcels-related restructuring costs are allocated to the Reserved Letters business.* • Australia Post is likely to be, and should be, undertaking ongoing restructuring in its parcels business and corporate head office, in addition to the Letters operations. • We share the concerns of ACCC/WIK-Consult that restructuring costs are not generally transparent, nor appropriately attributable/allocated to letters and parcels services.
	…that Australia Post undertake further work to address the issues raised by WIK Consult, such as:	***Desired Outcome:*** *The full costs of eDVs (including depreciation, maintenance, charging infrastructure, space within "Letters" facilities) along with their negative impact on Letters-related productivity, should be fully allocated to the Parcels business in order to*

	more closely considering incremental cost in cost causation and allocation regarding eDVs	*ensure that the full cost to deliver parcels is accounted for in Australia Post's pricing behaviour in the competitive parcels market.* • As noted by WIK-Consult, eDVs are being deployed for the purposes of enabling the delivery of more parcels by Posties. This has driven Parcels-related capital investment into the "Letters" network, but more importantly, it is also driving an increase in direct costs due to the subsequent fall of overall Postie productivity. We agree that the costs of eDVs, including the loss of productivity and facilities costs, should not under any circumstances be allocated to Reserved services.
	…that Australia Post undertake further work to address the issues raised by WIK Consult, such as: ***undertaking a program of work to assess whether there are direct and indirect benefits for non-reserved services that arise as a result of having <u>a larger Post Office network</u> and, accordingly, <u>adjust the method of allocating LPO subsidy costs…</u>***	***Desired Outcomes:*** ***1.*** *The costs of LPO subsidies and other relevant Post Office costs be proportionately allocated to the Parcels business based on the actual proportion of services performed by LPOs.* ***2.*** *Australia Post's management are better incentivised to genuinely consider opportunities to drive additional parcels-related revenue through Post Offices, including those able to be generated by providing a fee-for-service open access arrangement for other parcels providers to leave parcels at local community Post Offices for collection by consumers.* • Post Offices are now predominately providing non-letter services. • Parcel-related services (sending, collection, PO Boxes for parcels) are now one of the main services. • WIK-Consult has properly identified that the overall profitability issues of Reserved Letters services are being over-stated as a result of an over-allocation of Post Office network costs to those Reserved services.
	…that Australia Post undertake further work to address the issues raised by WIK Consult, such as: ***changing to a contractually specified transfer price system for cost allocations to StarTrack.***	• See note above regarding the urgent need for a clear, transparent and auditable transfer pricing regime addressing <u>**all**</u> commercial parcels carried by Australia Post's shared networks, irrespective of whether those parcels bear Australia Post or StarTrack-branding.
P62	***The ACCC recommends that Australia Post ensure their regulatory accounting procedures manual aligns with the classifications of reserved and non-reserved services under the Postal Act.*** *[…] Under these Record Keeping Rules, details from several schedules are required to be incorporated into Australia Post's regulatory accounting procedures manual.* ***This includes service group definitions for reserved and non-reserved services.*** *The Record Keeping Rules categorise inward international mail, apart from international inward letters,*	***Desired Outcome:*** *Given the serious implications for competition, we urge the ACCC to ensure that:* **1.** *Australia Post abides by this recommendation as a matter of high urgency,* **2.** *pricing of these products properly reflects the true and full cost to provide the services, and* **3.** *Australia Post is not competing unfairly in the international inbound market.* • The ACCC has correctly identified that international inward packets are not Reserved services and should therefore not be accounted for as such. • These articles are carried as commercial items and the allocation of the costs to handle these items to

	as non-reserved rather than reserved services. This is consistent with the definition of services which are not reserved under s 30 of the Postal Act. However, ***we have identified that Australia Post's 2023 regulatory account procedure manual currently lists <u>international inward packets</u> as reserved services.*** *The ACCC recommends Australia Post review their regulatory accounting procedures manual to ensure that the services classified as reserved or non-reserved are consistent with the Postal Act,* ***and that revenue and costs are attributed accordingly.***	Reserved services clearly serves to over-state the costs of providing Reserved services. • Furthermore, by not allocating costs to these commercial services in a proper way, it is highly likely that Australia Post's pricing of these products is below cost. This carries significant implications for competition in the international inbound market, where Australia Post already receives favourable regulatory treatment, despite operating in competitive markets.

We thank the ACCC for the opportunity to provide this submission and we are happy to provide any further information on request.

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