



Australian
Competition &
Consumer
Commission

Regulation Impact Statement

Record Keeping Rules establishing a regulatory accounting framework for Australian Post

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Australia Post

Australia Post is the government owned provider of postal services in Australia. It delivers approximately 5.2 billion articles of mail per year to 9.7 million delivery points. It was corporatised in 1989; this reform provided for an independent board and a commercial charter, albeit with ongoing obligations to meet community service obligations.

Australia Post's 'reserved' services

In recognition of its community service obligations, Australia Post has been granted a general monopoly—although this is limited by a number of exceptions—in the carriage and delivery of letters¹ within Australia. The services captured by this monopoly are generally referred to as 'reserved services'. The reserved services extend to:

- the collection, within Australia, of letters for delivery within Australia; and
- the delivery of letters within Australia.

Australia Post's non-reserved services

In addition to providing the reserved services, Australia Post provides a number of services in competition with other service providers. These include some letter services that fall within the exceptions to the general monopoly granted to Australia Post (such as letters weighing more than 250 grams)² and many other services including the sale of retail items in Australia Post outlets, over the counter financial and bill payment services, the provision of logistics and parcel delivery services.

In 2003–04, non-reserved services accounted for 55.4 per cent of Australia Post's revenue and 63.5 per cent of its profit from ordinary activities (before net interest and income tax).³

Role of the ACCC in regulating postal services

In addition to its general responsibilities in enforcing the *Trade Practices Act 1974*, the Australian Competition and Consumer Commission (the ACCC) has three specific responsibilities in the regulation of postal services:

- prices surveillance over Australia Post's reserved services, under Part VIIA of the Trade Practices Act

¹ The meaning of 'letters' in the Australian Postal Corporation Act is wider than its common usage, extending to any written communication that is directed to a particular person or address.

² Section 30 of the Australian Postal Corporation Act specifies the exceptions to the reserved services.

³ Australian Postal Corporation, *Annual report 2003–04*, p 85.

- inquiries into disputes about the terms and conditions on which Australia Post provides bulk mail services, under s.32B of the *Australian Postal Corporation Act 1989*
- monitoring for cross-subsidy between reserved and non-reserved services, under Part 4A of the Australian Postal Corporation Act.

To assist it in fulfilling these responsibilities, Part 4A of the Australian Postal Corporation Act allows the ACCC has to require Australia Post to keep records (and, on request, provide these records to the ACCC) about matters that are relevant to:

- the performance of the ACCC’s functions in relation to prices surveillance and to s. 32B of the Australian Postal Corporation Act
- the financial relationship between parts of Australia Post’s business that relate to reserved services and parts that do not
- the financial relationship between different parts of Australia Post’s business that relate to reserved services.

Problem identification

Some competitors of Australia Post, particularly newsagents, have alleged that Australia Post is unfairly competing in the market by using revenue from its reserved services to cross-subsidise its non-reserved services.

These allegations were investigated by the National Competition Council during its review of the Australian Postal Corporation Act during 1997–98. While the Council did not find any evidence to substantiate these allegations, it did recommend a requirement for detailed auditing and accounting information on Australia Post’s activities to provide for transparency of the financial relationships between different elements of its business as a safeguard against anticompetitive cross-subsidisation and inappropriate internal cost allocation between Australia Post’s activities.⁴

The Australia Government accepted this recommendation and sought to implement it by measures proposed in the Postal Services Legislation Amendment Bill 2000; however, this Bill was withdrawn.⁵

An alternative amendment, placing an obligation on the ACCC to require Australia Post to keep records about its reserved services ‘to enable the ACCC to scrutinise whether or not Australia Post is cross-subsidising from the reserved services to the

⁴ National Competition Council, *Review of the Australian Postal Corporation Act Final Report—Volume Two*, NCC, Melbourne, 1998, p 291.

⁵ Explanatory memorandum (incorporating the regulation impact statement) for the Postal Services Legislation Amendment Bill 2003, p. 4.

services it provides in competition with others', was introduced by the Postal Services Legislation Amendment Act.⁶ This obligation must be met by 22 June 2005.⁷

The record keeping rules establishing a regulatory accounting framework for Australia Post are intended to meet this obligation.

Objective

The objective of these record keeping rules is to provide the ACCC with sufficient information to allow it to scrutinise whether or not Australia Post is cross-subsidising from its reserved services to the services it provides in competition with others.

The information gathered under the record keeping rules will also be useful to the ACCC in fulfilling its other roles in the regulation of postal services.

Identification of options

Identifying cross-subsidy

In order to identify the recipient of a cross-subsidy, it is necessary to obtain estimates of the incremental cost of each service provided by Australia Post. Where revenue is less than the incremental cost of providing a particular service, that service is the recipient of a subsidy. In order to identify the source of a cross-subsidy, it is necessary to obtain estimates of the stand alone cost of each service provided by Australia Post. Where revenue is greater than the stand alone cost of providing a particular service, that service is the source of a subsidy.

Possible options

The ACCC has considered the following options, presented in order of perceived compliance cost to both Australia Post and the ACCC (from lowest to highest).

- Option 1** Require Australia Post to keep financial records about its reserved services only.

- Option 2** Require Australia Post to keep financial records on a historical cost and revenue basis using fully distributed costing for its two main service groups: reserved and non-reserved services.

- Option 3** Require Australia Post to keep financial records on a historical cost and revenue basis using fully distributed costing for a number of 'groups' of its services.

⁶ Explanatory memorandum for the Postal Services Legislation Amendment Bill 2003, p. 40.

⁷ Subsection 4(6) of the Postal Services Legislation Amendment Act.

- Option 4** Require Australia Post to keep financial records of stand alone and incremental costs and revenues for a number of its services.

Impact analysis

Specific cost to Australia Post of the reporting requirements

The record keeping rules will impose internal costs upon Australia Post to the extent that the rules require Australia Post to keep records that it would not otherwise keep.

The amount of these costs appears to be dependant upon:

- the degree to which the record keeping rules are consistent with Australia Post's existing accounting systems
- the level of disaggregation required by the record keeping rules.

Where the record keeping rules rely on Australia Post's existing systems, the cost is likely to be low; where the record keeping rules require the keeping and reporting of additional records that Australia Post does not currently keep, the costs will be higher.

Likewise, the greater the number of 'service groups' that Australia Post is required to report on, the greater will be the costs of complying with the record keeping rules.

Assessment of costs and benefits of alternative options

Option 1 Require Australia Post to keep records about its reserved services

This option would require Australia Post to keep records about its reserved services only. It is the least intrusive option available to the ACCC.⁸

However, this option would not meet the objective of the record keeping rules. That is, it would not provide the ACCC with sufficient information to allow the allegation of cross-subsidisation by Australia Post between its reserved and non-reserved services to be tested; it is necessary to obtain revenue and cost information about both the reserved and non-reserved services in order to identify the existence of cross-subsidy.

Option 2 Require Australia Post to keep financial records on a historical cost and revenue basis using fully distributed costing for its two main service groups: reserved and non-reserved services

This option would require Australia Post to keep records and report at an aggregated level for both its reserved and non-reserved services. It is therefore likely to have lower compliance costs for Australia Post when compared with options 3 and 4.

⁸ Subsection 50H(2) of the Australian Postal Corporation Act places an obligation on the ACCC to require Australia Post to keep records about its reserved services for the purpose of scrutinising whether or not Australia Post is cross-subsidising between its reserved and non-reserved services.

Reporting at this aggregated level would allow the ACCC to test for cross-subsidy; however, it would not be sufficient to allow the identification of cross-subsidy to a particular area within Australia Post's non-reserved services. For example, it is possible that non-reserved services as a whole are not the recipient of a subsidy, but that a particular service within the non-reserved services is the recipient of a subsidy.

Moreover, Australia Post already reports its financial performance at this level of disaggregation.⁹ That the Government has imposed an obligation on the ACCC to require Australia Post keep records indicates that it does not consider this level of disaggregation sufficient.

Option 3 Require Australia Post to keep financial records on a historical cost basis using fully distributed costing for a number of its services

This option would introduce accounting separation both between and within Australia Post's reserved and non-reserved services based on Australia Post's existing accounting system. Costs, revenues and non-current assets would be allocated to a number of 'service groups'¹⁰ that comprise all of Australia Post's specific goods and services. It would also require detailed description and 'account mapping' of Australia Post's cost allocations. The benefits of this option are:

- it provides for audited financial information
- it is based on Australia Post's existing accounting systems.

This option relies on Australia Post's existing accounting systems, thereby limiting Australia Post's costs to the additional requirements of the record keeping rules. These include producing regulatory accounts at a level of disaggregation that it may not otherwise produce, the identification of revenues, costs and assets that are direct, attributable or unattributable to particular service groups and the production of a regulatory accounting procedures manual that explains how the regulatory accounts were derived and provides details of how revenues, costs and assets were allocated to the various service groups.

Option 4 Require Australia Post to keep financial records of stand alone and incremental costs and revenues for a number of its services

Option 4 would require Australia Post to report the stand alone and incremental costs of providing its services (or particular groups of services, as was the case with Option 3).

Australia Post's accounting and financial systems are not currently configured to derive these types of costs (they are based on the fully distributed accounting costs) and would

⁹ Australia Post, *Annual Report 2003–04*, p. 85.

¹⁰ The number of service groups is a largely arbitrary decision: Australia Post provides a large number of services and requiring Australia Post to report on each one would be onerous, so some level of aggregation is necessary. The record keeping rules proposed under this option require Australia Post to report on 16 'service groups' (5 reserved and 11 non-reserved). During the public consultation all interested parties, including Australia Post, broadly supported this level of aggregation.

appear to require significant reconfiguring to be adapted to the concepts of incremental and stand alone costs (which are economic concepts).

Recommendation

The ACCC considered these options against the objective of the record keeping rules: to provide the ACCC with sufficient information to allow it to scrutinise whether or not Australia Post is cross-subsidising from its reserved services to the services it provides in competition with others.

The option that most likely to meet this objective without undue cost is Option 3.

Option 1 is not suitable because it would not provide the information required to test for cross-subsidy between the reserved and non-reserved services and would therefore not meet the objective of the record keeping rules.

Option 2, is also not suitable because, whilst providing more information than Option 1, it would allow for the testing of cross-subsidy at only the broadest possible level and would not necessarily identify whether a particular service was receiving a subsidy.

Option 4 would place significant compliance costs upon Australia Post because it would entail devising new estimates of costs, revenues and assets on a different basis to that which Australia Post currently keeps its records. This is likely to be prohibitively expensive.

Consultation

The ACCC engaged in significant consultation during the development of the record keeping rules.

The ACCC held discussions with Australia Post in August 2003 about the impending requirement for the ACCC to develop record keeping rules. The ACCC developed draft record keeping rules in the second half of 2003, with reference to other record keeping rules and accounting separation regimes administered by the ACCC and other postal regulators and with advice from KPMG on practical application. In March 2004 the ACCC released draft record keeping rules for public consultation.

The ACCC received four submissions in response to the draft record keeping rules and an associated Issues Paper. The submissions generally supported the regime proposed by the draft record keeping rules and, where it has considered appropriate, the ACCC has made changes to the record keeping rules.¹¹

Australia Post raised a number of particular issues that related to its accounting and financial policies; compliance costs; and confidentiality.

¹¹ ACCC, *Record keeping rules establishing a regulatory accounting framework for Australia Post—response to issues raised by submissions and other changes*.

New Zealand postal operators, Major Mail Users of Australia and the Post Office Agents Association made submissions that generally related to the transparency of the reporting procedures; compliance costs; confidentiality; and the level of segmentation required of Australia Post.

Since June 2004 the ACCC has been engaged in ongoing discussions with Australia Post regarding the record keeping rules and Australia Post has indicated that it supports the proposed record keeping rules.

Implementation and review

Implementation

The rules will come into effect on the date the record keeping rules are issued by the ACCC. The ACCC will issue them by providing an electronic copy to Australia Post and placing them on its web site. The ACCC will also make a public announcement that it has issued the rules.

Australia Post will be required to report to the ACCC annually (for the full financial year) under the proposed record keeping rules and has agreed to provide the first set of regulatory accounts for the 2004–05 financial year.

Review

The record keeping rules contain a review and amendment mechanism that enables both the ACCC and Australia Post to initiate changes to the record keeping rules:

- The ACCC may review and amend the rules from time to time, and when doing so it will consult with Australia Post and, where appropriate, seek public comment.
- Australia Post may request that the ACCC amend the rules. Consideration of such a request will be assessed against the objective of the rules, the requirements of the Australian Postal Corporation Act and any other relevant matters.

The ACCC intends to internally review the operation of the record keeping rules annually—after the regulatory accounts have been received and analysed. Where it considers it appropriate, the ACCC will consult (with Australia Post and more generally) on the application of the rules.