



ERGP (11) 17 Rev. 1 Annex – synthesis of the public consultation on the ERGP draft report on the Net cost of USO and VAT burden

## **Synthesis of the public consultation on the draft ERGP draft report on the Net cost of USO and VAT burden**

**August 2012**

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### **Summary of the results**

A public consultation of the ERGP draft report on net cost calculation and VAT burden was launched and took end on January 18th. Four contributions were received. Two of them came from national universal service providers, one from a postal operator and one from an economic consultant.

### **Issues covered**

#### **The tender procedure**

One contributor mention the difficulties related to the tender process. Relevant sector-specific conditions need to be considered such as changing behavior of customer's and industry structure. These have therefore to be thoroughly assessed.

#### **Cost calculation methodology**

One universal service provider finds that the most relevant approach for evaluating the net cost of universal service obligations would be the commercial approach, as it best fulfills the Directive's requirements for establishing the reference scenario, i.e. the situation where the USP has to deal without any universal service obligations. For the methodology to succeed the revenues that must be taken are only the ones that are directly connected to the USO (e.g. the VAT exemptions but not economies of scales which do not derive directly from US obligations).

Another national incumbent in charge of USO has an opinion on what would be the best method to evaluate the costs. Indeed the argumentation chooses the profitability cost approach which compares the operator's profits in the two scenarios. As argued, taking into account the real costs of the USP (top-down rather than a bottom-up model), is an exercise which is easier to establish and will also permit to avoid any cost inefficiency's compensation (assuming the same level of efficiency for both scenarios).

#### **The reference scenario**

Setting up a reference scenario is a part of the net cost calculation exercise that some contributors describe as a difficult task. Here again different assessments were made. For the postal operator, in the reference scenario, all of universal services will still be provided by the



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USP even without any obligation. The criterion to be modified is the tariff policy of the incumbent which will differ from one ex-universal service obligation from another, depending on the reaction of competition. Tariff regulation is also pointed out by another contributor to be the most restrictive obligation for the USP.

The economic consultant made it clear that the level of competition is one of the key elements of the reference scenario, as the demand and the USP's market power will evolve. Furthermore, choosing the services that the USP will still be willing to offer will affect the possibility for competitors to act on the market. This is why assuming the same level of competition in both scenarios is not accurate.

### **The VAT exemption**

For those who have contributed to the public consultation, the VAT exemption, as applied today, is a source of market distortions. A non-homogenous VAT system will not put the incumbent at the same playing field as competitors. The latter and potential new entrants' products will be charged with the VAT, and they will not be able to challenge the incumbent with competitive prices. However, this exemption may have a small but positive impact on consumer's surplus as the marginal tax rate level is lower when there is a VAT exemption system in place.

### **The unfair burden assessment**

Some criteria were given as propositions on how to define the unfair burden imposed by universal service provisions. The choice of any kind of criterion will directly depend on the aim of the compensation and the chosen financing mechanism.