



ERGP (13) 14 – common Position on cost allocation rules
synthesis of the public consultation

**Synthesis of the public consultation
on the draft ERGP common position on cost allocation rules
November 2012 - January 2013**

The ERGP submitted to public consultation its draft common position on cost allocation rules between 28 November 2012 and 23 January 2013.

The ERGP received replies from La Poste, PostEurop, Jantón Oy and UNI Europa Post & Logistics. These four responses are synthesized in this document; the final version of the opinion¹ takes into account the suggestions made to the ERGP regarding cost allocation rules. These responses are available at the following hyperlink: http://ec.europa.eu/internal_market/ergp/documentation/consultations_en.htm.

The ERGP appreciates all comments given and has integrated them into the report when appropriate. Nevertheless, some comments refer to issues not related to the ERGP mandate on cost allocation issues.

I. – The responses to the public consultation

La Poste notes that the ERGP takes into account the possibility to use the driver “urgency” to allocate costs. It also acknowledges that the definitions of direct costs, common costs and joint costs are clarified compared to the previous draft report. However, La Poste considers that this distinction is complex and not always relevant; the operator therefore recommends adopting a more economic approach by distinguishing fixed costs and variable costs. La Poste reasserts its position on the safeguarding of the universal service as the main priority.

PostEurop considers that the objective for regulators should no longer be a matter of introducing additional regulatory mechanisms in a fully liberalised market but ensuring adequate flexibility is left to incumbent operators to sustain appropriate universal service obligations. It stresses (noting, however, that the draft position does not seek to determine a common cost standard for regulatory purposes) that some proposed principles (p. 7, p. 18) seem to go far beyond what is requested by the postal directive (considering that the methodological principles for allocating costs are exhaustively described by art. 14 par. 3 of the directive) by providing the NRA with the possibility to pre-define the methodologies to be applied.

¹ http://ec.europa.eu/internal_market/ergp/documentation/documents_en.htm.

PostEurop considers that the principle of cost causation has to be better recognised in the final position and suggests emphasising that causality is the fundamental principle for cost allocation. It also recommends a clear statement that the basic principle for transfer prices is market price and, as an exception when no real market reference exists, that transfer prices should be cost oriented.

PostEurop insists on the fact that the cost accounting system is not the only relevant source for cost allocation, especially for the USO net cost calculation. As a consequence, it reckons that the second last paragraph of paragraph 0.III (p. 13) should be deleted or rewritten.

PostEurop finally finds that the ERGP position tends to widen the regulatory influence to business strategies and to extend the scope of regulatory reporting, accounting and audit far beyond the scope of the universal service and the requirements of the postal directive. According to PostEurop, this would be an excessive burden for the regulated companies and would lead to increased costs and to a competitive disadvantage.

Janton understands that regulation aims at protecting the availability and affordability of the universal service, although the latter covers only a part of the postal services. Janton believes that the most efficient way to ensure the availability of postal services is to promote competition in all the market segments. It deduces that the detection and prevention of abusive practices should be one of the main goals of the regulatory accounting which should include the costs and revenue from both regulated and non-regulated activities. It also considers that the cooperation between NRAs and NCAs should be reinforced in case of suspected abusive pricing practices by the incumbent.

Janton considers that the USO should not be regarded as a cost driver and that exceptions could be accepted only after making sure that they do not distort competition and that the resulting cost allocation does not lead to cross-subsidisation. It notes that network costs should always² be allocated to all products in proportion to the use of resources.

Janton believes that independent auditing and publication of the findings are an important part of the regulatory accounting. It suggests that the audit should cover all the (USO and non-USO) products, that the audit results should be made public to the greatest extent possible and that the auditor should not only be but also appear independent of the regulated operator – Janton asserts that independence cannot be guaranteed when the auditor is the same for both financial and regulatory accounts.

UNI Europa Post & Logistics (UNI) criticises regulation and pricing restrictions used as tools to artificially inject competition into the postal market at the disadvantage of the USP or incumbent operator. UNI stresses that many questions surrounding cost allocation rules will affect the provision of the universal service and the market position of the operators, two aspects influencing employment, working conditions and other social issues with which UNI is concerned.

² Janton adds that costs of an efficient operator could be taken into account in case any USO-specific network costs are accepted by the NRA.

UNI sees the question of cost allocation rules as one of general fairness in a liberalized market and supports the principle that the regulatory regime should not create inequality between operators in the postal market. In particular, UNI considers that cost allocation methods should accurately reflect the actual costs of providing the universal service and ensure that USPs are not disadvantaged by restrictions preventing them from competing in the market for non-universal service products.

II. – ERGP comments on the responses

II.1. – Scope of regulatory accounting

In its draft common position, the ERGP stresses on the totality principle. The latter requires the regulatory accounting to encompass any activity contributing to the provision of the universal service. This principle is regarded by the ERGP as a necessary step for cost allocation in line with paragraph 3. (iv) of article 14 of the Postal Directive, as implemented at the national level.

The ERGP reminds that, when requested, information shall be transmitted to NRAs in confidence and that NRAs shall preserve such confidentiality. Therefore, financial information communicated by operators shall receive an appropriate treatment.

The draft common position also highlights the possibility, subject to national legal provisions, for NRAs to set the methodological principles which specify the high-level accounting and costing rules. As noticed by respondents, this solution shall be implemented without prejudice to the article 14 of the Directive.

Regarding internal transfer charges:

- The cost base evaluation of internal transfer charge should always be available within the accounting system as a reference;
- However, if helpful for preventing inefficiency, discrimination or price squeeze, market prices when available may be used, for example to set prices of universal services;
- Reconciliation of regulatory accounts with the statutory accounts is crucial.

The ERGP finally notes Janton position on a necessary cooperation between NRA's and NCA's.

The final common position is therefore modified to take into account the following points:

- NRAs shall treat financial information communicated by the operator as confidential, in order to prevent any competitive disadvantage;
- the methodological principles are set by the NRAs, without prejudice of the article 14 of the Directive;
- the cost base evaluation of internal transfer charge should always be available within the accounting system as a basic reference; market prices should be used for transfer prices only where appropriate;
- the legal provisions for a cooperation between NRAs and NCAs.

II.II. – Allocation rules

The ERGP notes PostEurop reluctance regarding the proportionality principle. On this issue, as stated in points 8 and 9 of the Executive summary and p. 26 of the draft common position, *“The principle of cost causality applies. [...]. Specific allocation rule: In some cases, specific cost allocation rules could be considered to reduce common costs [...].”* The concern about cost causality principle is taken into account in the ERGP final common position:

“The principle of cost causality applies. Cost drivers should cover technical relationships between products and activities. In this regard, the universal service obligation should not automatically be regarded as a cost driver. For the USO to be treated as such, evidence should be provided by the USP and formally acknowledged by the NRA.”

Proportionality and causality principles are not at odds. When a cost driver exists, then they coincide, otherwise the principle of proportionality would lead to allocation of this cost with a general allocator.

In this view, the cost causality principle is in line with the proportionality principle and remains a fundamental principle that must apply for cost allocation. The proportionality cannot always be sufficient for cost allocation in cases of products sharing joint costs, though. In these cases, the use of the causality principle enables limitations to the proportionality principle to be overcome, by making relevant costs allocation compatible with the article 14(3) of the Directive.

Regarding the cost allocation rules of the network, and more precisely the existence of a USO-specific network cost, the annex 1 of the Directive suggests the consideration of efficiency for this type of cost. As announced in its 2013 work program³, this question will be subject of further investigation by the ERGP.

Finally, the draft common position states that *“Although net cost calculation is not produced exclusively by the accounting system (since it is necessary to evaluate avoided costs and lost revenues in a counterfactual scenario), for the calculation to be well grounded, it is crucial to correctly identify the relevant costs and revenues.”*

If a regulatory accounting is not designed to evaluate the costs and revenues in a counterfactual scenario, it could however provide relevant information regarding USO products in the current situation of the operator. Therefore, the regulatory accounting rules and methodology can be a key input for a net cost evaluation, without being the only relevant source.

³ http://ec.europa.eu/internal_market/ergp/docs/documentation/2012/ergp-12-37-final-work-programme_en.pdf

The final common position is clarified on the matter of the link between regulatory accounting and the USO net cost evaluation.

II.III. – Auditing procedure

The ERGP notes PostEurop reluctance regarding the extent of the regulatory audit beyond the USO scope. On this issue, the ERGP reminds that this extension shall cover only the products affected by the totality principle.

The final common position is clarified on this matter.

II.IV. – Additional issues

The responses of La Poste, PostEurop and UNI stress on the issue of USO sustainability that should lead, according to the respondents, to fewer regulatory mechanisms. The ERGP is committed to the safeguard of the universal service. However, the common position is focusing on the issue of cost allocation, especially common costs between USO and non-USO products, in a market fully opened to competition, hence the principles and rules presented in this document.