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Assessing cross-subsidy in Australia Post

2014–15

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Glossary

ACCC	Australian Competition and Consumer Commission
APCA	<i>Australian Postal Corporation Act 1989</i>
attributable cost	costs that are part of a pool of common costs identifiable to a particular service by a separable cause-and-effect relationship
Australia Post	Australian Postal Corporation
cross-subsidy	a cross-subsidy occurs where profits from the supply of a service are used to cover a loss incurred in the supply of another service
CCA	<i>Competition and Consumer Act 2010 (formerly Trade Practices Act 1974)</i>
direct cost	costs that are solely associated with a particular service and so are incremental to providing that service
fully distributed cost	the sum of direct, attributable and unattributable costs allocated to the particular service or group of services
incremental cost	the additional cost incurred by producing a good or service (in addition to the other goods the firm produces)
non-reserved services	services not subject to Australia Post's statutory monopoly (i.e. generally, services it provides in competition with other businesses)
PreSort letters	Australia Post's PreSort letter service is a bulk mail service that provides discounted prices for business customers that barcode and sort their letters prior to lodgement
RAF	regulatory accounting framework
record-keeping rule (RKR)	a requirement by the ACCC that Australia Post keep certain records
regulatory accounts	the statement of financial performance, statement of capital employed, statement of movements in non-current asset values, statement of WACC and statement of service group usage required by the RKRs to be provided by Australia Post to the ACCC
reserved services	postal services reserved to Australia Post under the APCA legislation (i.e. no other entity can provide these services)
segment	For the purpose of compliance with the ACCC's regulatory accounting framework, Australia Post combines service groups into broader 'segments'. Australia Post's segments in 2014–15, were Mail (reserved and non-reserved), Parcels, Retail and agency and Other services
service group	the service groups defined in Schedule 1 of the RKR information provided by Australia Post (for example, consumer and financial products is a service group)
stand-alone cost	the cost of producing each output or service in isolation
unattributable cost	a cost that is part of a pool of common costs but is not readily identifiable (in whole or part) to any particular service by a separable cause-and-effect relationship
UPU	Universal Postal Union
WACC	weighted average cost of capital

Key Messages

- The ACCC has a number of postal regulatory responsibilities including assessing proposals for price increases for the basic postage rate. However this report deals only with the ACCC's role in assessing cross-subsidy by Australia Post.
- The ACCC uses regulatory accounts submitted by Australia Post to conduct economic tests to assess whether Australia Post is using revenue from its monopoly letter service to cross-subsidise those services it provides in competition with other businesses.
- Any cross-subsidy by Australia Post from its reserved (statutory monopoly) services to its non-reserved services would be a concern because Australia Post could damage competition in other markets by the use of its legislated monopoly.
- The ACCC's cross-subsidy testing has found that Australia Post did not use profits from its monopoly reserved letter services to unfairly compete in other markets in 2014-15.
- The ACCC is satisfied that Australia Post's monopoly letter services were not a source of subsidy in 2014-15. Australia Post's monopoly letter services were unable to recover their operating costs, so they were a potential recipient of a subsidy. The level of cost recovery of reserved services has been declining together with letter volumes since 2007-08.
- In fact, prior to 2013-14, it has been non-reserved services that have been a source or a potential source of subsidy for the reserved services. However, in 2014-15, no specific non-reserved service was a definite source of subsidy. Furthermore, Australia Post's non-reserved services (as a whole) in 2014-15 were also a potential recipient of a subsidy (when adjusted for the cost of capital).
- The results of the ACCC's cross-subsidy testing also reflect a continued decline in Australia Post's financial performance. In 2014-15, Australia Post reported its first ever operating loss. A significant factor affecting Australia Post's cost recovery in 2014-15 is a \$200 million provision for restructuring costs associated with the reform of its letters business.

1. Introduction

The ACCC has a role under the *Australian Postal Corporation Act 1989* (APCA) to assess whether Australia Post is cross-subsidising its non-reserved services (generally, services it provides in competition with others) with revenues from its reserved (statutory monopoly) services. This would be a concern because Australia Post could damage competition in competitive markets by the use of its legislated monopoly.¹

To undertake its cross-subsidy assessment, the ACCC relies on information provided by Australia Post in its regulatory accounts. The regulatory accounts provide detailed revenue and cost information disaggregated by defined service groups. For example:

- Direct costs are solely associated with a particular service (for example, cost of goods sold can be directly attributed to products sold in Australia Post's retail stores). Due to the shared and labour-intensive nature of Australia Post's operations, it has very few direct cost items relating to specific mail services.
- Attributable cost items are part of a pool of common costs that are identifiable to a particular service by a separable cause-and-effect relationship. For example, the labour costs associated with processing and delivering letters can be described as attributable.
- Unattributable costs are part of a pool of common costs but are not readily identifiable to any particular service. For example, costs associated with senior management and central support functions such as finance and corporate affairs are classified as unattributable costs.

The regulatory accounts must be prepared by Australia Post in accordance with an ACCC record keeping rule (RKR). Australia Post allocates revenues, costs, and assets between service groups using its cost allocation methodology (CAM). The regulatory accounts are reviewed by an independent auditor who audits Australia Post's compliance with the RKR and Australian Auditing Standards. The ACCC does not formally review Australia Post's CAM as part of its annual cross-subsidy assessment process.

However, as part of its assessment of Australia Post's price notification in 2015, the ACCC employed WIK Consult (Wik) to review the CAM. The Wik review did not identify any systematic bias in Australia Post's CAM but did identify some areas where further improvements could be made to the CAM. As discussed in Section 2.6, Australia Post has committed to working with the ACCC to further improve its CAM in particular so that it more accurately reflects cost differences between ordinary and stamped priority letter services.

Each year in undertaking this cross-subsidy analysis, the ACCC has adjusted the regulatory accounts submitted by Australia Post to allow for a return on capital. The ACCC considers a return on capital is a legitimate cost to business. Accordingly the conclusions and cross-subsidy tests results in this report are presented on a capital-adjusted basis, unless otherwise noted. However, as discussed in Appendix A, cost figures presented in Section 4 of this report do not include a return on capital. This approach allows readers to reconcile the figures presented with Australia Post's annual report, and recognises Australia Post's claim of confidentiality over its weighted average cost of capital (WACC) and its components.

The remainder of this report is structured as follows:

- Section 2 provides an overview of Australia Post and the ACCC's roles in the regulation of postal services
- Section 3 outlines the ACCC's framework for monitoring for cross-subsidy
- Section 4 sets out the results of the ACCC's cross-subsidy analysis for 2014–15

Appendix A outlines Australia Post's cost allocation methods, accounting policies, and general notes about the presentation of the cross-subsidy results in this report.

¹ A monopolist may be able to sustainably maintain prices below cost in related markets using profits from its monopoly services. In such a situation, customers that use the monopoly services are charged higher prices that contain a subsidy for the customers that use the monopolist's competitive services. This may result in economically inefficient over-consumption of non-reserved services, and may also negatively affect the competitiveness of the non-reserved service market. Additionally, in such a situation an economic inefficiency arises because prices for the monopoly services are, on the whole, at higher than competitive levels.

2. Background

The ACCC has a number of postal regulatory responsibilities including assessing price increases in the basic postage rate (currently \$1). However this report deals only with the ACCC's role in assessing cross-subsidy by Australia Post.

This report presents the results of the ACCC's analysis of Australia Post's regulatory accounts for the 2014-15 financial year in order to determine whether Australia Post cross-subsidised its contestable services with revenue from its monopoly letter services.

The ACCC was given this role in 2004 in response to complaints by competitors that Australia Post was damaging competition by cross-subsidising its contestable services with revenues from its reserved services. In June 2004 the APCA was amended to provide for the ACCC to issue a RKR that would 'enable the ACCC to scrutinise whether or not Australia Post is cross-subsidising from reserved services to the services it provides in competition with others'.²

This section provides an overview of Australia Post's obligations in providing postal services and the ACCC's role in the regulation of postal services.

2.1 Australia Post's functions and obligations

Australia Post is the government-owned provider of postal services in Australia.

At the end of 2014-15, Australia Post employed approximately 36 700³ people and operated 4 406 retail outlets.⁴ In 2014-15 Australia Post delivered mail to 11.4 million Australian addresses with 98.8 per cent of these receiving letter delivery five days a week.⁵

The APCA requires that Australia Post:

- as far as is practicable, performs its functions in a manner consistent with sound commercial practice⁶
- meet certain community service obligations (outlined below)⁷
- perform its functions in a way consistent with general government policy and any directions given by the Minister.⁸

Australia Post has a community service obligation to supply a letter service. The purpose of the letter service is to carry, by physical means, letters within Australia and between Australia and places outside Australia.

For letters that are standard postal articles, Australia Post must make the letter service available at a single uniform rate of postage for carriage within Australia. In recognition of the social importance of the letter service, Australia Post must ensure that:

- the letter service is reasonably accessible to all people on an equitable basis, wherever they reside or carry on business
- the performance standards of the letter service reasonably meet the social, industrial and commercial needs of the Australian community.

2.2 Services 'reserved' to Australia Post

In recognition of its community service obligations, Australia Post has a general monopoly in the carriage and delivery of letters within Australia, subject to some specific exemptions.⁹

2 Explanatory memorandum for the *Postal Services Legislation Amendment Bill 2003*, p. 40. Section 50H(2) of the APCA provides the ACCC with authority to require Australia Post to keep certain records about its reserved services.

3 Australia Post annual report 2014-15, p. 1.

4 Australia Post annual report 2014-15, p. 1.

5 Australia Post annual report 2014-15, p. 27.

6 Section 26 of the APCA.

7 Section 27 of the APCA.

8 Section 28 of the APCA.

9 Section 27 of the APCA.

The services covered by this monopoly are generally referred to as 'reserved services'. They extend to:

- the collection within Australia of letters for delivery within Australia
- the delivery of letters within Australia.

The term 'letters' has a meaning that is wider than its general usage—the APCA defines 'letter' as meaning any form of written communication that is directed to a particular person or a particular address.¹⁰

Australia Post also has the exclusive right to issue postage stamps within Australia.

As noted above, the monopoly in relation to reserved services is subject to a number of exceptions, which are detailed in section 30 of the APCA. Some of these include:

- the carriage of a letter weighing more than 250 grams
- the carriage of a letter relating to goods that is sent and delivered with the goods
- the carriage of a newspaper, magazine, book, catalogue or leaflet, whether or not directed to a particular person or address and whether or not enclosed in any sort of cover
- the carriage of a letter otherwise than for reward
- the carriage of a letter on behalf of a foreign country under a convention
- the carriage of a letter within Australia for a charge or fee that is at least four times the then rate of postage for the carriage within Australia of a standard postal article by ordinary post.

2.3 ACCC role in the regulation of postal services

The ACCC has three key roles in the regulation of postal services under the *Competition and Consumer Act 2010* (CCA) and the APCA. This report deals only with one of these roles, under which the ACCC has the power to issue record keeping rules (RKR) requiring Australia Post to keep certain records.¹¹

The ACCC also has two other roles under the CCA and the APCA:

- assessing proposed price increases of Australia Post's notified¹² services under Part VIIA of the CCA
- inquiring into certain disputes regarding the terms and conditions on which Australia Post supplies its bulk mail services.¹³

2.4 Record-keeping rule powers

In March 2005 the ACCC issued an RKR that established a regulatory accounting framework (RAF) for Australia Post. In accordance with this RKR, Australia Post has submitted regulatory accounts to the ACCC for each financial year from 2004–05. The primary purpose of the RAF is to allow the ACCC to assess whether Australia Post is cross-subsidising losses incurred by the services it provides in competition with others with profits from its reserved services.

The ACCC may prepare and publish reports—or may be directed by the Minister to prepare and publish reports—analysing information provided to it under the RKR.¹⁴ Such reports may include information that Australia Post claims is commercial-in-confidence if:

- the ACCC is not satisfied that the claim is justified; or
- the ACCC considers it in the public interest to publish the information.¹⁵

¹⁰ Section 3 of the APCA.

¹¹ Section 50H of the APCA.

¹² In 2015, the Australian Government limited price surveillance of Australia Post letter services to certain letter services reserved to Australia Post. For example, the \$1 basic postage rate (BPR) and other Ordinary letter services carried at the new 'regular' timetable remain 'notified' and thus subject to price notification requirements. The other services currently reserved to Australia Post such as PreSort letters are no longer notified. Refer *Price Notification Declaration (Australia Post Letter Services) (No 2) 2015*.

¹³ Regulations made under section 32B of the APCA allow the ACCC to inquire into disputes about the terms and conditions, including price of access to Australia Post's bulk mail services.

¹⁴ Sections 50I and 50J of the APCA.

¹⁵ Sections 50K of the APCA.

2.5 Australia Post's Cost Allocation Model

Australia Post has an extensive collection and delivery network which it uses to provide its mail services. Australia Post's reserved monopoly letter services are a subset of services Australia Post provides using its collection and delivery network. For example, non-reserved services provided by Australia Post, including express post and parcels, are also provided using elements of this network.

Australia Post applies a CAM to allocate shared costs across its business for reserved and non-reserved services. Within reserved services the CAM is also applied to help derive prices for the various monopoly services.

2.6 Wik review of Australia Post's cost allocation model (CAM)

The ACCC engaged an external consultant with expertise in the postal industry, Wik, to review Australia Post's CAM in 2015 as part of its assessment of Australia Post's price notification. Wik previously reviewed Australia Post's CAM in 2008 and that review led to a number of improvements to the CAM.¹⁶

The 2015 Wik review considered:

- the reasonableness of the allocation of Australia Post's direct and shared costs between reserved and non-reserved services including regular and priority letter services
- the appropriateness of the CAM given relevant accounting standards, the trend of declining letter volumes and increasing parcel volumes, and current and future cost differences in the delivery of regular and priority letter services
- the extent to which the CAM provides a reasonable model to derive efficient costs and prices for regular and priority letter services
- potential improvements that could be made to the CAM.

In undertaking this task Wik considered Australia Post's Regulatory Accounts for the 2013–14 financial year.¹⁷ Wik also visited Australia in August 2015 to attend meetings with Australia Post and conduct site visits at Australia Post's letter processing and delivery centres.

Wik's review did not identify any systematic bias in Australia Post's CAM that would lead to an over allocation of costs to reserved services from non-reserved services but did identify some issues with the CAM.¹⁸ Australia Post has committed to working with the ACCC to further improve its CAM in particular so that it more accurately reflects cost differences between ordinary and stamped priority letter services.

¹⁶ A non-confidential summary of the 2008 Wik review of Australia Post's CAM is available on the ACCC website at http://www.accc.gov.au/system/files/20080529_wik_AustraliaPost_CostAllocation_Summary.pdf.

¹⁷ Australia Post's 2013–14 Regulatory Accounts were the latest available at the time the Wik review was conducted. These accounts provide a separation of revenues and costs between Australia Post's reserved and non-reserved businesses and are used by the ACCC for monitoring the presence of cross subsidies between Australia Post's reserved and non-reserved services.

¹⁸ A report of the 2015 Wik review of Australia Post's CAM is available on the ACCC website, <https://www.accc.gov.au/system/files/WIK%20Cost%20Allocation%20Model%20Review%20-%20Full%20Report.PDF>

3. Framework for monitoring for cross-subsidy

The term ‘cross-subsidy’ is often used to refer to any case where the profit from providing one service is used to cover a loss incurred in providing another service.

In monitoring for the presence of cross-subsidies from the monopoly reserved services to the contestable non-reserved services, the ACCC seeks to identify whether the revenue from any non-reserved service group is less than the incremental cost of providing that service group and whether the revenue generated by reserved services is greater than the stand-alone cost of providing them.

As discussed in Section 3.1 below, in assessing Australia Post’s regulatory accounts for the presence of cross-subsidy, the ACCC relies on accounting proxies for economic stand-alone and incremental costs.

The assessment of whether a cross-subsidy occurs is independent of the question of the efficiency of Australia Post’s costs, which the ACCC has historically considered as part of its price notification assessments.

3.1 Economic vs accounting costs

The ACCC considers that Australia Post would be likely to incur significant compliance costs if it were required to keep financial records on the economic cost concepts of stand-alone and incremental costs. Such a requirement would entail devising new estimates of costs, revenues and assets on a different basis to the one Australia Post currently uses to keep its accounting records.¹⁹

Accordingly, the incremental and stand-alone costs referred to in this report are based on accounting data and provide a proxy for what the true economic incremental or stand-alone costs may be. The cost proxies used by Australia Post are direct, attributable and unattributable costs:

- **direct account items** are solely associated with a particular service and will be incremental to providing that service
- **attributable account items** are part of a pool of common account items that are identifiable to a particular service by a separable cause-and-effect relationship
- **unattributable account items** are part of a pool of common account items but are not readily identifiable (in whole or part) to any particular service by a separable cause-and-effect relationship.

These cost proxies are described in more detail in Appendix A.1.

3.2 Testing for cross-subsidy

Cross-subsidies occur when one group of users pay for more than the costs of the services they receive, and the surplus is used to offset the cost of services provided to other users. They may occur as an unintended result of the chosen charging mechanism or deliberately (to pursue equity or social policy objectives for example).

Cross-subsidies between different processes or different users may permanently disadvantage one group relative to another. Those who pay the subsidy may restrict their use of the product, reducing desirable consumption that would have taken place if products were appropriately priced. Conversely, those who receive a subsidy may be encouraged to use too much of the product.

The rationale for the ACCC’s role in assessing cross-subsidy in Australia Post is that it may use cross-subsidies from its legislated monopoly in the provision of letter services to damage competition in competitive markets. If a monopolist is able to cross-subsidise its contestable services by revenues from its monopoly services this may damage competition in the markets in which it competes, because the monopolist is able to sustainably maintain prices in those markets below cost using profits from its monopoly services. In such a situation, customers that use the monopoly services maybe charged higher prices that contain a subsidy for the customers that use the monopolist’s competitive services. This may result in economically inefficient over-consumption of non-reserved services, and may also negatively affect the competitiveness of the non-

¹⁹ ACCC, *Regulation impact statement, record keeping rules for establishing a regulatory accounting framework for Australia Post*, March 2005, p. 6.

reserved service market. Additionally, in such a situation an economic inefficiency arises because prices for the monopoly services are, on the whole, at higher than competitive levels.

The formal definition of cross-subsidy that has developed in the economic literature comprises two tests that compare a service's revenues to different cost concepts.²⁰

The first is the stand-alone cost test for whether a service is a **source** of cross-subsidy:

- The stand-alone costs are defined as the costs that an efficient competitor would incur in providing just that service or group of services.
- In testing Australia Post's regulatory accounts for cross-subsidy, the lower bound of the stand-alone cost test is assumed to be the service's fully distributed cost (i.e. the sum of the service's direct, attributable and unattributable costs). Where the service's revenue exceeds fully distributed cost, it may be a source of subsidy.
- The upper bound of the stand-alone cost test is assumed to be the sum of the service's direct and attributable costs, and the total of all of Australia Post's unattributable costs. Where the service's revenue is above this upper bound, it is a definite source of subsidy.

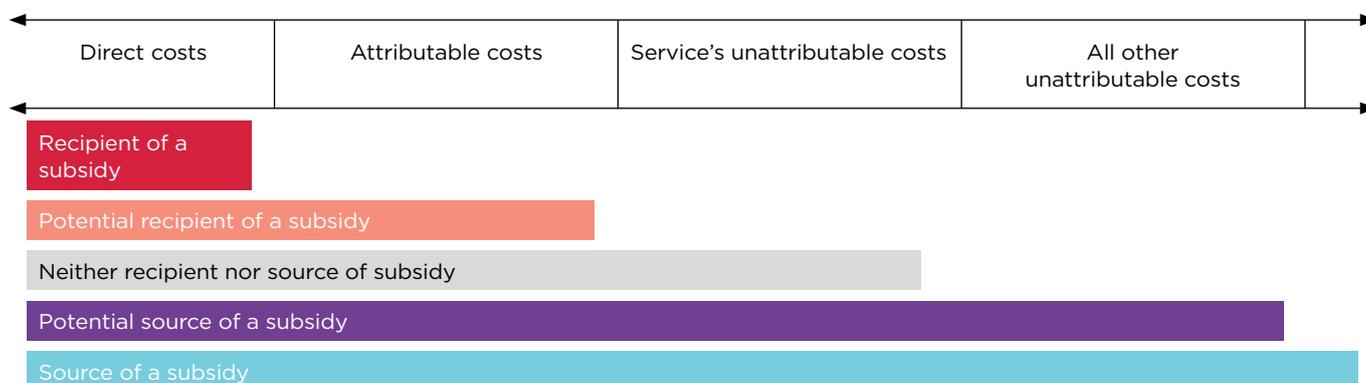
The second test is the incremental cost test for whether a service is a **recipient** of cross-subsidy:

- Incremental costs are the additional costs incurred by the monopolist in providing just that service or group of services. Another way of considering incremental cost is to ask 'what costs would be avoided, in the long run, if the service was no longer offered?'
- In respect of testing Australia Post's regulatory accounts for cross-subsidy, where revenue is less than direct costs, the service is a recipient of a subsidy. This is the lower bound of the incremental cost test.
- Where revenue is sufficient to cover the direct costs, but less than the sum of direct and attributable costs, the service group is assumed to be a possible recipient of a subsidy. This is the upper bound of the incremental cost test.

The range of possible cross-subsidy results is presented graphically at Chart 3.1 below.

Chart 3.1 Range of possible cross-subsidy results

Service revenue recovers:



Further details about how the ACCC applies these cross-subsidy tests is outlined in the document titled 'ACCC tests for assessing cross-subsidy in Australia Post' which is available on the ACCC website at <http://www.accc.gov.au/publications/assessing-cross-subsidy-in-australia-post>.

20 GR Faulhaber, 'Cross-subsidization: pricing in public enterprises', American Economic Review, 65(5), December, 1975, pp. 966-77.

4. Analysis of Australia Post's 2014–15 accounts

This section sets out the results of the ACCC's analysis of Australia Post's regulatory accounts for 2014–15. Australia Post's current business structure has four business groups:

- Mail services: The collection, processing and distribution of mail items. This is comprised of:
 - reserved mail - the collection, processing and distribution of domestic letters defined as reserved by the APCA
 - non-reserved mail - the processing and distribution of non-reserved domestic letter services
- Parcel services: The processing and distribution of parcel and express products along with freight forwarding operations.
- Retail and agency services: Providing services across identity, digital, receiver and agency service offerings, as well as the sale of financial and retail merchandise products, principally philatelic, stationery, telephony, greeting cards, gifts and souvenirs.
- Other services: This includes services that are incidental to Australia Post's core products and services, principally those which generate rental income, license fees, and other miscellaneous amounts.

The ACCC has applied the incremental cost test and the stand-alone cost test to each of the service groups, and the broader segments. The overall conclusion based on Australia Post's regulatory accounts, after taking into account capital costs, is that the non-reserved services did not receive a subsidy from reserved services. Revenue from reserved services was not sufficient to cover the lower or upper bound of the stand-alone costs test, which needs to be met for a service to be a potential source of subsidy.

The ACCC is therefore satisfied that reserved services were not a source of subsidy.

In 2014–15, Australia Post's financial position was affected by significant provisions for future redundancies, and the company reported its first ever operating loss. The provisions mainly relate to Australia Post's letters business, which is in decline, and its reserved letter services in particular. In fact, Australia Post's overall revenues were less than its operating costs. This is the first time Australia Post has been unable to recover its operating costs since the ACCC started monitoring for cross-subsidy in 2004–05. The level of cost recovery of reserved services has been declining together with letter volumes over time, which has increasingly affected the ability of the overall business to recover its costs. For example, in 2013–14 Australia Post also did not recover all of its costs (after a capital adjustment).

The following table presents the cross-subsidy test results for 2014–15 based on the products and service types specified in Australia Post's 2014–15 regulatory accounts. As discussed in Appendix A.2, the test results outlined below were performed using capital-adjusted costs—that is, Australia Post's accounting costs were adjusted to include a rate of return on the capital employed for each service group. The ACCC does not endorse Australia Post's proposed weighted average cost of capital (WACC) either for the purposes of cross-subsidy analysis or for other purposes—such as a price notification. Nor does the ACCC endorse the various input parameters used by Australia Post in its statement of WACC. However, a lower WACC, such as that used in the ACCC's decision on the 2015 price notification, does not affect the ACCC's key finding in this report which is that Australia Post's reserved services were not a source of subsidy for its non-reserved services. Accordingly, it is not necessary for the ACCC to determine a precise WACC for current purposes.

Furthermore, the test results are generally robust whether or not the capital adjustment occurs (i.e. in most cases the capital adjustment only affects the size of the subsidy).

Adjusting the results for capital (based on Australia Post's proposed WACC) does not affect the result of cross-subsidy test for each of the service groups in 2014–15. However, adjusting for capital does affect the testing for non-reserved services, mail services and non-letter services as a group.

On a capital-adjusted basis non-reserved services and mail services are potential recipients of a subsidy, while on a non-capital adjusted basis these services are neither the recipient or source of subsidy. Similarly, non-letter services are on a capital-adjusted basis neither a recipient or source subsidy but are a potential source of subsidy on a non- capital-adjusted basis.

Despite use of the capital-adjusted costs in testing, all dollar cost figures in this section of the report are reported on a non-capital adjusted basis. This approach allows readers to reconcile the figures presented

with Australia Post's annual report, and recognises Australia Post's claim of confidentiality over the information contained in the statement of capital employed.

Table 1: Results of 2014–15 cross-subsidy tests on a capital adjusted basis

	Is the service group a recipient of a subsidy? (Revenues less than incremental costs)		Is the service group a source of a subsidy? (Revenues greater than stand-alone costs)	
	Definitely	Potentially	Definitely	Potentially
	(revenues less than the lower bound of incremental cost: i.e. direct costs)	(revenues less than the upper bound of incremental cost: i.e. direct and attributable costs)	(revenues greater than the upper bound of stand-alone cost: i.e. fully distributed costs plus all other unattributable costs)	(revenues greater than the lower bound of stand-alone cost: i.e. fully distributed costs)
Total reserved mail	NO	YES	NO	NO
small letters ordinary	NO	YES	NO	NO
large letters ordinary	NO	YES	NO	NO
small letters PreSort	NO	YES	NO	NO
large letters PreSort	NO	YES	NO	NO
Total non-reserved mail	NO	YES	NO	NO
large letters ordinary	NO	NO	NO	YES
large letters PreSort	NO	YES	NO	NO
other letter mail services	NO	YES	NO	NO
Total parcels	NO	NO	NO	YES
international outward letters	NO	NO	NO	YES
international inward letters	NO	YES	NO	NO
parcels	NO	NO	NO	YES
international outward parcels	NO	NO	NO	YES
international inward parcels	NO	YES	NO	NO
StarTrack and Express	NO	NO	NO	YES
Total retail and agency	NO	NO	NO	YES
consumer and financial products	NO	NO	NO	YES
government and agency services	NO	NO	NO	YES
Total other services	YES	YES	NO	NO
Total reserved services	NO	YES	NO	NO
Total non-reserved services	NO	YES	NO	NO
Total letter services	NO	YES	NO	NO
Total non-letter services	NO	NO	NO	NO
Total mail services	NO	YES	NO	NO
Total non-mail services	NO	YES	NO	NO

4.1 Did any service group receive a subsidy in 2014–15?

Revenue for the following services in Australia Post's submitted 2014–15 regulatory accounts did not recover the direct and attributable costs of providing them, and the services were therefore recipients of a subsidy or potential recipients of a subsidy in 2014–15:

- international inward letters (non-reserved) (Section 4.1.1)
- international inward parcels (non-reserved) (Section 4.1.2)
- large PreSort letters (non-reserved) (Section 4.1.3)
- other letter mail services (non-reserved) (Section 4.1.4)
- other services (non-reserved) (Section 4.1.5)
- small ordinary letters (reserved) (Section 4.1.6)
- large ordinary letters (reserved) (Section 4.1.6)
- small PreSort letters (reserved) (Section 4.1.6)
- large PreSort letters (reserved) (Section 4.1.6)

4.1.1 International inward letters (non-reserved)

Payment for the delivery of most international mail is overseen by the Universal Postal Union (UPU) under a system known as 'terminal dues'. The terminal dues payable to the destination postal operator are not based on the actual costs incurred in delivering this mail. Rather, terminal dues remuneration is linked to a formula that uses a percentage of the basic postage rate.

Revenues from the international inward letters were below the direct and attributable costs of providing these services in 2014–15. Previous cross-subsidy reports showed that while there was an under-recovery of fully distributed costs in international inward letters, international outward letters over-recovered its fully distributable costs for each of the years the ACCC has been monitoring cross-subsidy.

International letters as a group (both international inward and outward letters) recovered its fully distributed costs in 2013–14 and 2014–15, which had not occurred since 2004–05. This is partially due to increased terminal dues, which took effect from 1 January 2015.

4.1.2 International inward parcels (non-reserved)

The inward international parcels service group relates to the receipt, handling, delivery and on-forwarding of inbound international parcels and related mail articles within Australia. For small parcels (i.e. less than 2kg) the remuneration Australia Post receives for these services is determined by the terminal dues system.

Revenue from the international inward parcels was below the direct and attributable costs of providing the services in 2014–15.

According to Australia Post, the performance of the service group is dependent on parcel volumes, the \$A/SDR exchange rate and domestic delivery costs.

Australia Post has advised that the decline in the performance in this service group has been due to a shift in volume mix towards the parcels less than 2kg category, which forms part of the terminal dues stream. The recent decline in the Australian dollar has negatively impacted volumes in this category.

4.1.3 Large PreSort letters (non-reserved)

This service relates to the collection and delivery of letters which fall within the weight and price definition of an Ordinary Large Letter – non-reserved²¹, but where the customer has undertaken a sorting exercise to organise the letters according to pre-defined criteria by Australia Post.

The service, like most of Australia Post's letter services, was a potential recipient of a subsidy in 2014–15.

4.1.4 Other letter mail services (non-reserved)

The 'other letter mail services category contains a range of non-reserved letter services, such as Unaddressed Mail and Periodicals.

²¹ Letters weighing more than 250 grams and that are priced at least four times the basic postage rate are non-reserved services.

This service group was a potential recipient of a subsidy in 2014–15. Australia Post has advised that this is due to the fact that, compared to volume, revenue for the service group is proportionally lower as it contains some low unit revenue products such as Unaddressed Mail.

4.1.5 Other services (non-reserved)

'Other services' is a category used by Australia Post that relates to non-product-specific operations of Australia Post's business, so there is no direct relationship between revenues, costs, profit and asset allocations. Revenue from 'other services' includes miscellaneous revenue that cannot be attributed to other products, such as property rents, license fees and other revenue such as unclaimed money orders. Costs under 'other services' consist of an allocation of corporate overheads and include property management for external leases. Assets purchased for future use are also included under 'other services'.

This service was a recipient of a subsidy on both a non-capital and capital-adjusted basis. Australia Post advises that the reason for this is that there was an increase in operational and administration expenses, and costs relating to real estate due to vacant building space not let.

4.1.6 Reserved services

In 2014–15, revenue from each of Australia Post's four reserved letter services was below their respective direct and attributable costs. The individual letter service trends are summarised below.

- Small ordinary letter services have failed to recover their fully distributable costs since the ACCC began monitoring cross-subsidy in 2004–05. Revenue from small ordinary letters was below direct and attributable costs in each of the years from 2005–06 to 2014–15. The recovery of direct and attributable costs has generally been decreasing since the ACCC began monitoring cross-subsidy, which may reflect the decline in letter volumes experienced in recent years.
- Revenue from large ordinary letter revenues was also less than fully distributable costs, meaning that these services were a potential recipient of subsidy in 2014–15. Prior to 2013–14, this service has been able to recover its fully distributable costs and has been a potential source of subsidy.
- Small PreSort letter services failed to recover their fully distributable costs in each of the years from 2007–08 to 2014–15. Revenue from small PreSort letters had been above the direct and attributable costs of providing these services from 2004–05 to 2008–09, but from 2009–10 to 2014–15 the service did not recover its direct and attributable costs.
- Large PreSort letter revenues have failed to recover fully distributed costs in each of the years from 2008–09 until 2014–15. In 2009–10, 2010–11, and 2012–13 to 2014–15 the service also under-recovered its direct and attributable costs.

In summary, the ACCC's cross-subsidy analysis shows that each of the four reserved letter services potentially received a subsidy in 2014–15. However the ACCC's cross-subsidy assessment is focused on detecting the situation where Australia Post is able to cross-subsidise its contestable services by revenues from its monopoly services. Such a situation may damage competition in the markets in which Australia Post competes, because it is able to maintain prices in those markets below cost. This situation does not arise when the reverse form of cross-subsidy occurs (i.e. where contestable services on the whole appear to be subsidising the monopoly services), or where the business as a whole does not recover all of its costs.

4.2 Are reserved services a source of subsidy?

In 2014–15, there were no reserved service groups which were able to recover fully distributed costs, or even their respective direct and attributable costs. The reserved services as a whole also did not recover their total direct and attributable costs. Thus, they were not a source of subsidy, but a potential recipient of a subsidy.

Table 2 shows the 2014–15 revenue and cost recovery for total reserved services in comparison to total non-reserved services prior to a capital adjustment (2013–14 revenues and costs are provided for context).

The fully distributed cost of reserved services is likely to underestimate the actual stand-alone cost of providing these services. In that case it is necessary to add back some of the unattributable costs that were allocated to non-reserved services (i.e. the unattributable costs that may be incurred by Australia Post whether non-reserved services were provided or not). However, identifying the appropriate amount to be added back is problematic. As discussed in Section 3, one approach is to establish an upper bound on the

stand-alone cost. This could be done by adding back all the unattributable costs that were allocated to all other services. Since reserved services revenue was substantially lower than the fully distributed costs of providing reserved services, adding back other unattributable costs will only increase the under-recovery.

Table 2: Reserved and non-reserved services revenues and costs (\$million) on a non-capital-adjusted basis

	2013-14 reserved services	2013-14 non-reserved services	2014-15 reserved services	2014-15 non-reserved services
Revenue	1771.2	4463.4	1734.7	4545.8
Direct cost	6.0	1607.9	5.0	1976.9
Attributable cost	1943.3	2380.2	1872.6	2371.8
Unattributable cost	64.5	186.9	143.2	277.4
Fully distributed cost	2013.8	4175.0	2020.7	4626.2
Revenue less direct cost	1765.2	2885.4	1729.7	2568.8
Revenue less direct and attributable costs	(178.1)	475.2	(142.8)	197.0
Revenue less fully distributed cost	(242.6)	288.3	(286.0)	(80.4)
Revenue less fully distributed cost and all other unattributable costs	(429.5)	223.8	(563.5)	(223.6)

The ACCC has also applied the stand-alone cost test to other groups of services in order to identify possible sources of subsidy.

Table 3 shows the cost recovery in 2014-15 for all of Australia Post's business segments (prior to a capital adjustment). The parcels and retail and agency services segments were the only two business segments able to recover their fully distributed costs, which means that they were potential sources of subsidy. However, neither segment had revenue sufficient to recover all the unattributable costs allocated to all other services, so neither was a definite source of subsidy.

Table 3: Australia Post's revenues and costs by segment totals (\$million) on a non-capital-adjusted basis

	Reserved letter services	Non-reserved mail services	Parcels	Retail and agency services	Other services
Revenue	1734.7	340.2	3207.0	1012.3	(13.7)
Direct cost	5.0	0.5	1209.4	388.5	378.6
Attributable cost	1872.6	400.1	1608.1	363.5	-
Unattributable cost	143.2	28.9	144.4	115.2	(11.0)
Fully distributed cost	2020.7	429.5	2961.9	867.2	367.6
Revenue less direct cost	1729.7	339.7	1997.6	623.9	(392.3)
Revenue less direct and attributable costs	(142.8)	(60.4)	389.4	260.3	(392.3)
Revenue less fully distributed cost	(286.0)	(89.3)	245.1	145.1	(381.3)
Revenue less fully distributed cost and all other unattributable costs	(563.5)	(481.1)	(31.2)	(160.3)	(812.9)

4.3 Total letter services and total mail services

Although Australia Post does not have a legislated monopoly for non-reserved letter services, it nonetheless has a strong market position in these areas due to its wide-ranging collection and distribution networks. Accordingly, to identify possible sources of subsidy, the ACCC has applied the stand-alone cost test to both total letter services and total non-letter services.

Table 4 shows that revenue from total reserved and non-reserved letter services was less than the direct and attributable costs of providing these services, so they were a potential recipient of a subsidy. Australia Post's total non-letter services as a whole were a potential source of subsidy, prior to a capital adjustment.

Table 4: Letter and non-letter revenues and costs (\$million) on a non-capital-adjusted basis

	Total letter services	Total non-letter services
Revenue	2074.9	4205.6
Direct cost	5.5	1976.5
Attributable cost	2272.7	1971.7
Unattributable cost	172.1	248.5
Fully distributed cost	2450.2	4196.7
Revenue less direct cost	2069.4	2229.1
Revenue less direct and attributable costs	(203.3)	257.5
Revenue less fully distributed cost	(375.4)	8.9
Revenue less fully distributed cost and all other unattributable costs	(623.9)	(163.1)

Table 5 shows that, prior to a capital adjustment, revenue from aggregate letter and parcel services was greater than the direct and attributable costs but less than the fully distributed costs of providing these services.

Table 5: Letter and parcel and non-letter and non-parcel revenues and costs (\$million) on a non-capital-adjusted basis

	Total letter and total parcel services ³¹	Total non-letter and non-parcel services
Revenue	5281.9	998.6
Direct cost	1214.9	767.1
Attributable cost	3880.8	363.5
Unattributable cost	316.4	104.2
Fully distributed cost	5412.1	1234.8
Revenue less direct cost	4067.0	231.6
Revenue less direct and attributable costs	186.2	(132.0)
Revenue less fully distributed cost	(130.3)	(236.1)
Revenue less fully distributed cost and all other unattributable costs	(234.5)	(552.6)

In contrast, revenue from aggregate non-letter and non-parcel services was less than the direct and attributable cost, so it was a possible recipient of a subsidy. This group is comprised of 'retail services' which was a potential source of subsidy and 'other services', the non-product category, which was a recipient of a subsidy.

4.4 Cross-subsidy assessment over time

The following section outlines the general trends over the ten years that the ACCC has been conducting its cross-subsidy analysis.

The level of cost recovery of reserved services has been declining together with letter volumes over time. A ten-year time-series of the results of the ACCC's cross-subsidy tests on Australia Post's regulatory account data is presented in table 6. Note that changes to Australia Post's accounting policies, and in particular the classification of service groups, will impact on comparison of results over time.²²

²² For more information on the ACCC's historical tests, and on material changes to Australia Post's accounting policies refer to ACCC cross-subsidy reports for 2004-05 to 2013-14 (available on the ACCC website).

Table 6: Results of cross-subsidy tests from 2005–06 to 2014–15 on a capital adjusted basis

Service group	2005–06	2006–07	2007–08	2008–09	2009–10	2010–11	2011–12	2012–13	2013–14	2014–15
Total reserved mail										
Total non-reserved mail										
Total parcels services										
Total retail and agency										
Total other services										
Total reserved services										
Total non-reserved services										
Total letter services										
Total non-letter services										
Total mail services										
Total non-mail services										
TOTAL										

LEGEND

Recipient of a subsidy	
Potential recipient of a subsidy	
Neither recipient nor source of a subsidy	
Potential source of a subsidy	
Source of a subsidy	

4.4.1 Total business

Australia Post reported an operating loss for the first time in 2014–15.²³ Australia Post has been unable to recover its full costs (operating costs and capital costs) on only two occasions, in 2009–10 and 2013–14.²⁴

4.4.2 Broad business area

Australia Post’s business operation can be categorised into a number of broad areas where there is a similarity of products sold and/or the services provided.

- *Reserved services* have been neither recipient nor source of a subsidy from 2005–06 to 2008–09 and a potential recipient of a subsidy from 2009–10 to 2014–15. In general, the cost recovery of reserved services has been declining together with letter volumes.
- *Non-reserved services* have been a source of subsidy from 2005–06 to 2008–09 and from 2010–11 to 2012–13, a potential source of subsidy in 2009–10 and neither recipient nor source of a subsidy in 2013–14. It was a potential recipient of a subsidy in 2014–15.
- *Letter services* (reserved and non-reserved) as a whole have been potentially a source of subsidy from 2005–06 to 2007–08, neither the recipient nor source of a subsidy in 2008–09 and a potential recipient of a subsidy from 2009–10 to 2014–15. Like reserved letters, letter services’ cost recovery has followed the downward trend of overall letter volumes.
- *Non-letter services* as a whole have been a source of subsidy from 2005–06 to 2006–07 and from 2010–11 to 2012–13 and a potential source of subsidy from 2007–08 to 2009–10 and in 2013–14. It was neither the recipient or source of a subsidy in 2014–15.
- *Mail services* (includes letters and parcels services) were a potential recipient of subsidy in 2013–14 and 2014–15. Mail services were previously a source of subsidy from 2005–06 to 2008–09 and neither recipient nor source of a subsidy from 2009–10 to 2012–13.
- *Non-mail services* (all services except letters and parcels services) have been potentially a source of subsidy in all previous years the ACCC has been monitoring cross-subsidy. In 2014–15 it was a potential recipient of a subsidy.

23 A significant factor affecting Australia Post’s profitability in 2014–15 is the \$200 million provision for restructuring costs associated with the reform of its letters business.

24 In 2009–10, Australia Post’s regulatory accounts were affected by \$150 million of restructuring costs.

4.4.3 Service group

Australia Post has a number of service groups which it reports on in its regulatory accounts. These services groups are either reserved or non-reserved services.

- *Reserved mail services*: see 'reserved services' above.
- *Non-reserved mail services* segment have been a potential source of subsidy from 2005–06 to 2010–11 but were a potential recipient of subsidy from 2011–12 to 2014–15.
- *Parcels services* segment has been potentially a source of subsidy from 2005–06 to 2010–11 and from 2013–14 to 2014–15, and were a definite source of subsidy from 2011–12 to 2012–13.
- *Retail and agency services* have been a potential source of subsidy in all years the ACCC has been monitoring cross-subsidy with the exception of 2012–13 when it was a source of subsidy.
- *Other services'* segment has been a potential source of subsidy in 2005–06 and 2006–07, a potential recipient of a subsidy in 2007–08 and 2008–09, neither the recipient nor source of a subsidy in 2009–10, and a recipient of a subsidy from 2010–11 to 2014–15.

Appendix A: Accounting policies and cost allocation

The results of the cross-subsidy assessment will be affected by:

- the method of allocating costs to service groups (Section A.1)
- Australia Post's accounting policies (Section A.2)

The ACCC has made a number of changes in the way it presents the cross-subsidy results in 2014–15. These changes are discussed in Section A.3.

A.1 Cost allocation

The ACCC does not formally review Australia Post's activity-based cost allocation methodology (CAM) as part of its annual cross-subsidy assessment process.

To undertake its annual cross-subsidy assessment, the ACCC uses information provided by Australia Post in its regulatory accounts, which are required to be prepared in accordance with the ACCC's RKR. The regulatory accounts are reviewed by an independent auditor who audits Australia Post's compliance with the RKR and Australian Auditing Standards.

Australia Post allocates revenues, costs, and assets between service groups using its CAM. Australia Post is required by the RAF to provide revenue and cost information (regulatory accounts) disaggregated by defined service groups and reported as direct, attributable or unattributable account items.

Direct account items are account items that are solely associated with a particular service and will be incremental to providing that service (for example, cost of goods sold can be directly attributed to products sold in Australia Post's retail stores). Due to the shared and labour-intensive nature of Australia Post's operations, it has very few direct account items relating to its mail services (for example, most of the delivery costs would be shared by a number of mail and small parcel services, and are attributed to the product by the cost allocation methodology).

Attributable account items are part of a pool of common account items that are identifiable to a particular service by a separable cause-and-effect relationship. For example, the labour costs associated with processing and delivering letters can be described as attributable, as these costs are attributed to particular mail and parcel services based on their revenues, volumes, and the relative effort of delivery/processing the product.

Unattributable account items are part of a pool of common account items but are not readily identifiable (in whole or part) to any particular service by a separable cause-and-effect relationship. For example, costs associated with senior management and central support functions such as finance and corporate affairs are classified as unattributable items. Unattributable account items are allocated to particular service groups using some factor (such as, for example, relative use).

The ACCC engaged an external consultant with expertise in the postal industry, Wik, to review Australia Post's CAM in 2015 as part of its assessment of Australia Post's price notification. Australia Post acknowledged the comments by the ACCC and Wik and committed to working with the ACCC in relation to its cost allocation model, and in particular regarding the accurate reflection of regular and priority cost differences. The key findings of the 2015 review are discussed in Section 2.6 of this report.

A.2 Australia Post's accounting policies

Australia Post's 2014–15 regulatory accounts have been prepared to be consistent with, and are reconcilable with, the company's annual report. The financial accounts in Australia Post's annual report comply with Australian Accounting Standards.²⁵

²⁵ Australia Post annual report 2014–15, p. 62–63.

A.2.1 Accounting for a return on capital

In conducting the tests discussed in Chapter 4 of the report, the ACCC used a 'capital-adjusted' statement of financial performance.²⁶ The ACCC believes a return on capital is a legitimate cost to business.²⁷ As part of the ACCC's cross-subsidy assessment the cost of capital is included in the cross-subsidy tests. Accordingly, in seeking to identify the existence of cross-subsidy, it is appropriate to identify and quantify this cost.

The ACCC has applied the tests for cross-subsidy on both a capital-adjusted and a non-capital-adjusted basis and found that the results are generally robust whether capital adjustment is made or not. That is, adding a return on capital as a cost does not in most cases affect whether there is a subsidy, but only the magnitude of the subsidy.

The ACCC does not endorse Australia Post's rate of return on capital (WACC) proposed in its statement of WACC either for the purposes of cross-subsidy analysis or for other purposes (such as a price notification). Nor does the ACCC endorse the various input parameters used by Australia Post in its statement of WACC. The ACCC notes that a lower WACC, such as that used in the ACCC's decision on the 2015 price notification, does not affect the ACCC's key finding in this report which is that Australia Post's reserved services were not a source of subsidy for its non-reserved services.

While the conclusions presented in this report are generally presented on a capital-adjusted basis, dollar figures presented in this report have not been adjusted to reflect a return on capital. This approach allows readers to reconcile the figures presented with Australia Post's annual report, and recognises Australia Post's claim of confidentiality over the capital employed figures.

A.2.2 Changes to Australia Post's accounting policy

As required under the RKR, Australia Post has provided the ACCC with details of material changes to the accounting policies it implemented between the submission of the 2013-14 regulatory accounts and the 2014-15 regulatory accounts.

Organisational restructure

The structure of the 2014-15 regulatory accounts has been updated to align to Australia Post's current business structure. Overall the four operating segments in Australia Post's 2014-15 regulatory accounts are broadly similar to the segments contained in the 2013-14 regulatory accounts. Australia Post's current business structure has four business groups:

- Mail services: The collection, processing and distribution of mail items. This is comprised of:
 - reserved mail - the collection, processing and distribution of domestic letters defined as reserved by the APCA
 - non-reserved mail - the processing and distribution of non-reserved domestic letter services
- Parcel services: The processing and distribution of parcel and express products along with freight forwarding operations.
- Retail and agency services: Providing services across identity, digital, receiver and agency service offerings, as well as the sale of financial and retail merchandise products.
- Other services: This includes services that are incidental to Australia Post's core products and services, principally those which generate rental income, license fees, and other miscellaneous amounts.

The services categorised in the business segments above are similar to 2013-14 with the exception of Other Letters Associated, Other Non Product, StarTrack International, and Courier services. The products have been realigned to different segments in the current period to better reflect the way business unit results are analysed internally.

- 'Other Letters Associated' (mail services) is no longer reported as a separate service and has been consolidated into 'Consumer and Financial Products' and 'Other Non Product' services

²⁶ The WACC is applied to the value of capital employed for each service group, and this cost of capital is added to the statement of financial performance to derive a 'capital-adjusted' statement of financial performance for each of the service groups.

²⁷ ACCC, *Issues raised during consultation: Record-keeping rules establishing a regulatory accounting framework for Australia Post*, March 2005 (published on the ACCC website), p. 3.

- 'Courier services' (parcel services) is no longer reported as a separate service and has been consolidated into 'StarTrack & Express'
- The previous 'StarTrack International' (parcel services) service group has been renamed to 'StarTrack & Express' in line with current internal reporting. Courier services and certain parcel products such as express have been incorporated in the new service group.
- The previous 'Retail' service group has been renamed to 'Consumer and Financial Product' in line with current internal reporting. In addition certain, certain products have been realigned to different segments in the current period to better reflect the way business unit results are analysed internally.
- The previous 'Financial Services' service group has been renamed to 'Government & Agency services' in line with current internal reporting. In addition certain, certain products have been realigned to different segments in the current period to better reflect the way business unit results are analysed internally.

Network Cost Allocation Update (NCAU)

Australia Post continually reviews its CAM in line with business changes. The most recent review of methodology has focused on network cost allocations – the Network Cost Allocation Update (NCAU)

NCAU was set up to review and update the CAM's operational cost allocation drivers to reflect the reforms and changes to the business in the network, and obtain newly available sources of operational data.

NCAU commenced by verifying letter and parcel network activities and then updated, included or excluded activities to reflect current business operations. For example, vans have traditionally been used in the clearance of letters from street posting boxes, but are now used to also pick up customer parcels.

Australia Post expects that NCAU will result in a more accurate allocation of costs between reserved and non-reserved services.

A.3 Presentation of cross-subsidy results

A.3.1 Australia Post's new business units

Changes to Australia Post's accounting policies, and in particular the classification of service groups, will impact on comparison of results over time.²⁸ For example, as noted above at A.2.2, in 2014–15 the classification of a number of service groups was changed by Australia Post.

The 2014–15 cross-subsidy report presents the cross-subsidy results consistently with Australia Post's current organisational structure to ensure that the cross-subsidy results are reconcilable with Australia Post's annual report and segment note.

A.3.2 International inward and outward letters

In this report, the ACCC has changed the categorisation of international inward and outward letters. Previous cross-subsidy reports have grouped these services as part of the broad category of 'letter services'. Given that Australia Post categorises international inward and outward letters as part of the 'Parcels' group, in the 2014–15 cross-subsidy report these services have been included in 'non-letter services', which includes other parcels services.

A.3.3 Reply Paid fees

In 2014–15 Australia Post included 'Reply Paid fees' for the first time as a reserved service. This service is defined by Australia Post as a fee charged for reply paid services such as Reply Paid Letters (Domestic). An annual fee of \$100 applies for every domestic Reply Paid permit, which is charged to a customer's account.

The ACCC considers that these fees are not a reserved service and has included these fees under 'other letter mail services', a non-reserved service. In future, Australia Post has agreed to classify this service as a non-

²⁸ Refer to ACCC cross-subsidy reports for 2004–05 to 2013–14 (available on the ACCC website) for details of changes to accounting policies over time.

reserved service (under 'other letter mail services') to reflect the fact that the fee would not be covered by the statutory monopoly.

A.3.4 Inter-segment fees

Australia Post's annual and regulatory accounts included 'Inter-segment fees' as a service for the first time in 2014-15. Australia Post has noted that inter-segment costs and revenues are a way of establishing an internal transfer price between the Mail, Parcel and Retail and agency segments, equivalent to the market price paid to the licensed post offices for distributing mail and parcel products.

The ACCC has excluded the inter-segment costs and revenues from its cross-subsidy testing in 2014-15 as the inclusion of 'inter-segment fees' (which include significant negative revenue and negative cost components) would have produced non-meaningful cross-subsidy results.