Australian Government

Department of Communications

Regulation Impact Statement for proposed reforms to postal regulation

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Status of the RIS

The Australian Government announced reforms to the postal regulatory framework on 3 March 2015. These reforms require amendments to the *Australian Postal Corporation (Performance Standards) Regulations 1998* and the *Price Notification Declaration (Australia Post Letter Services) (No. 2) 2011*. The amended instruments will be tabled in Parliament and subject to disallowance.

This Regulation Impact Statement (RIS) contains details regarding the:

- challenges facing Australia Post;
- necessity of Australian Government action;
- policy options considered;
- likely net benefits of each option;
- consultation undertaken;
- reform option selected by the Australian Government, and announced on 3 March 2015; and
- implementation and review of the agreed regulatory reforms.

Background

Australia Post's reserved letter services

Under the *Australian Postal Corporation Act 1989* (the APC Act), Australia Post has the exclusive right to collect, carry and deliver letters within Australia that (subject to exceptions) weigh not more than 250 grams. This letters monopoly, along with the right to issue postage stamps, is Australia Post's 'reserved services'[1]. Australia Post was given this statutory monopoly so that revenue from its reserved services could fund the cost of meeting its Community Service Obligations (CSOs)[2]. The CSOs require Australia Post to supply a letter service that is 'reasonably accessible to all people in Australia on an equitable basis, wherever they reside or carry on business'[3]. In particular, the letter service must be available at a single uniform rate for standard letters carried by ordinary post.

Within the reserved services, Australia Post offers a number of different categories of mail. Ordinary letter services are offered at three postage prices—currently $0.70 for small letters (the Basic Postage Rate – BPR), $1.40 for large letters up to 125 grams, and $2.10 for large letters over 125 grams and up to 250 grams. Australia Post also offers 'other letter services', including 'bulk mail', that are used mainly by businesses, government agencies and not-for-profit organisations, and which are generally offered at prices lower than those of equivalent ordinary letter services.

Australia Post's commercial obligations

Section 26 of the APC Act requires Australia Post to, as far as practicable, perform its functions in a manner consistent with sound commercial practice. As a Government Business Enterprise (GBE), a principal objective for Australia Post is to earn at least a commercial rate of return.

[1] Division 2 of Part 3 of the APC Act
[2] The 1989 explanatory memorandum for the APC Act stated: 'The right to carry letters within Australian and between Australia and overseas is reserved to Australia Post in recognition of the CSOs imposed on Australia Post.'
[3] See Division 1 of Part 3 of the *Australian Postal Corporation Act 1989* (APCAct)

This includes fully recovering the costs of resources employed, including capital, and working towards a financial target and a dividend policy agreed with shareholder ministers. The rate of return should be at least sufficient to justify the long-term retention of assets in the business, and to pay commercial dividends from those returns[4].

Regulatory oversight

Australia Post has regulatory obligations in relation to the delivery of letters, with letter delivery standards detailed in the *Australian Postal Corporation (Performance Standards) Regulations 1998*. The standards specify, among other things, the speed, frequency and accuracy of letter delivery.

Australia Post is also subject to oversight by the Australian Competition and Consumer Commission (the ACCC) over the pricing of the BPR, and must notify the ACCC if it proposes to increase the price of a reserved letter service. The Minister for Communications has the power, under section 33 of the APC Act, to disapprove the proposed increase within 30 days after receiving notice from Australia Post.

Further detail on Australia Post's regulatory framework is at **Attachment 1**.

1. The problem

Australia Post is facing serious and ongoing challenges to its continued financial sustainability, which have arisen as a result of two related factors:

a) the continuing and accelerating decline in the volume of letters being carried and delivered, which is causing losses in Australia Post's letters business due to the fixed cost nature of Australia Post's operations; and
b) the domestic postal regulatory environment which restricts Australia Post's ability to respond to the letter volume decline.

In 2014, The Boston Consulting Group (BCG) examined the challenges facing Australia Post and possible regulatory and operational reforms to improve Australia Post's ability to respond to these challenges. The analysis focussed on the letters service. Deloitte Access Economics was also engaged to provide analysis of the economic impacts of each reform option.

Declining letter volumes

The postal services market is undergoing a fundamental transformation due to the increasing availability and sophistication of digital alternatives to the existing letters business. In essence, Australia Post is competing with email, social networking and online promotion and transaction channels. All sectors of society are adopting these alternative communications mechanisms, taking advantage of the efficiencies they offer in terms of convenience, cost and speed of service. For example, Australia is the sixth most concentrated smartphone market in the world after Singapore, South Korea, Norway, Spain and Sweden[5] with over 12 million Australians using a smartphone as at

[4] *Commonwealth Government Business Enterprise Governance and Oversight Guidelines*, Department of Finance and Deregulation, 2011, para. 1.8
[5] Deloitte Mobile Consumer Survey 2014 – The Australian Cut: Revolution and evolution

May 2014[6]. The higher the ubiquity of smartphones, the more Australians are transacting services and communicating over the Internet.

As a result, Australia Post is facing a decline in the volume of letters. The total volume of addressed letters carried by Australia Post has declined from a peak of around 4.6 billion in 2007-08 to around 3.4 billion in 2013-14 (a reduction of around 25%) as shown in the **Table 1**:

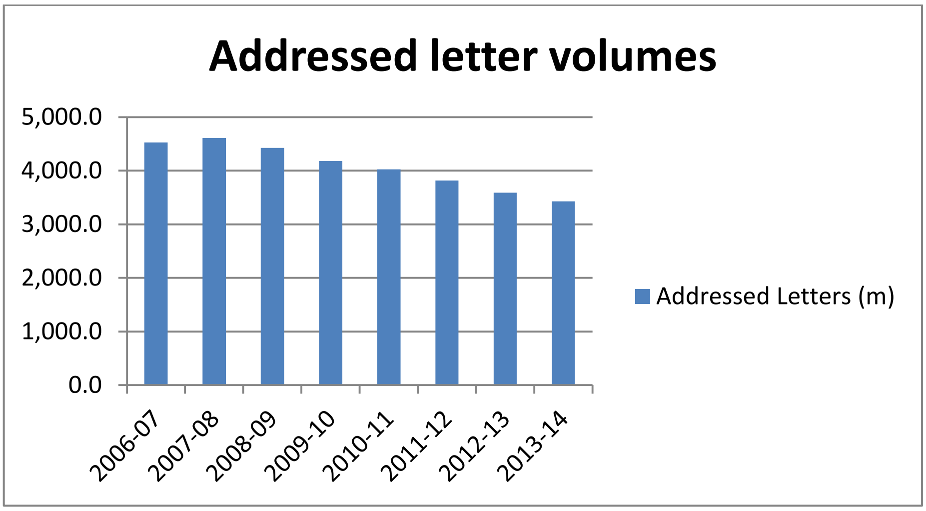


Table 1: Domestic addressed letter volumes

Australia Post is forecasting that, consistent with the experience of overseas postal service providers, the rate of decline in letter volumes will continue to accelerate. As at March 2015 the year-to-date decline in letters volume is 7.6%, which is consistent with BCG's estimate of letter volumes decline of 7% – 9% per annum to 2016-17[7].

It is not clear that there is a "floor" at which letter volumes will stabilise. This is especially the case as the impetus towards digital channels of communication is increasing, with businesses and governments (which send approximately 95% of all letters) seeking to deliver more services digitally. For example, the Australia Government has established[8] a Digital Transformation Office (DTO) to transform the way government services are delivered, including:

- making all new and redesigned services digital by default;
- ensuring all new and redesigned services can be completed digitally from start to finish on any mobile device; and
- expanding the use of the myGov digital mailbox, enabling users to receive correspondence from the Government digitally.

In 2013–14, 5.6% of all business and government letters were sent by federal government agencies. This is a 14.0% decline from the previous year.

[6] Australian Communications and Media Authority Communications report 2013–14
[7] Australian and International Postal Services Overview Background Report, Boston Consulting Group (BCG)
[8] http://www.minister.communications.gov.au/malcolm_turnbull/news/joint_release_with_the_hon_tony_abbott_mp,_prime_minister_establishment_of_a_digital_transformation_office#.VTheT42KCUn

As a result of the decline in letter volumes, the letters business has made a trading loss every year since 2008-09. It lost $218.4 million in 2012-13[9] and $328.4 million in 2013-14. Losses are forecast to reach $300 million in 2014-15, following a first half loss of $151 million.

If realised, future losses could result in Australia Post finding it difficult to access external funding. In this case, Australia Post may be forced to divest non-letters business units (e.g. its parcels business) to obtain funds to continue to meet its CSO. Prudent management may mean it seeks Budget supplementation as early as 2016-17. If the point is reached when all available sources of funds are exhausted, Australia Post would cease operations or require an equity injection from the Australian Government.

To date, Australia Post has been able to offset letters losses by growing its parcels business to subsidise financial losses in letters. This has enabled Australia Post to continue to return a profit and pay dividends to the Australian Government. In addition, Australia Post has undertaken a range of cost-cutting initiatives across the organisation, but it is reaching the limits of cost reductions that can be made without impacting on its ability to meet the CSOs.

The National Commission of Audit (NCOA) noted that ongoing decline in letter volumes "presents a major risk to the Budget and a risk to the continued delivery of postal services to the public, without reform of Australia Post's CSOs and cost structure, and/or privatisation." The NCOA also noted that there is "a strong case for considering options for reforming Australia Post's mandate and business operations[10]."

Restrictive postal regulations

Stamps in Australia are the cheapest in the OECD with only three other OECD countries offering stamps below $1.00. However, Australia also has one of the largest and, therefore, most expensive delivery networks in the world.

The regulatory framework governing Australia Post was developed before the Internet became ubiquitous, offering cheaper and more immediate substitutes to letters. The regulations were also established in an environment where letter volumes were increasing on a continual basis, and a primary objective of the regulations was to establish consumer safeguards in a market where Australia Post had a monopoly.

The importance of the letters service to the economic health of the nation is diminishing and the relevance and importance of the CSOs is likewise declining. However, despite the impact of digital substitution, Australia Post still carried 3.4 billion addressed letters in 2013-14, with continuing reliance by business and governments on letters for transactional and promotional material.

Removal of the CSOs (as one element of deregulation of the postal market) would significantly impact consumers in regional communities. Such a move is unlikely to result in the introduction of significant competition in the delivery of letters and small parcels in regional Australia, due to the significant distances, high costs and relatively low volumes involved.

[9] Australia Post Annual Report 2012-13
[10] Appendix to the Report of the National Commission of Audit, Volume 2, February 2014

In addition, Australia Post may be subject to "cherry picking" in profitable elements of its network, and seek to increase prices on other parts of the network to maintain revenues, further disadvantaging its customers.

Any removal of the CSO requirements would ideally follow a broad-ranging inquiry into the expected benefits and costs of maintaining the CSOs.

Australia Post is facing a significantly altered operating environment, with letter volumes in steep decline and its letters service experiencing increasing operating losses. While appropriate in the past, the postal regulatory framework has not been revised to respond to the increasing availability and sophistication of digital alternatives to the existing letters service, such as the Internet, online and text messaging, and smart mobile devices. The regulations impose significant and increasing costs on Australia Post and limit its freedom to respond to changing market conditions.

Australia Post's CSO costs have increased over time, to $203.5 million in 2013-14[11]. Since 2008–09, Australia Post's domestic reserved letter services as a whole have operated at a loss and this cost has effectively been met from Australia Post's non-reserved mail business and other commercial activities[12].

The requirements in relation to speed and frequency of delivery have a major impact on Australia Post's costs, approximately 80% of which are fixed[13].

In November 2014, ratings agency Standard & Poor's lowered Australia Post's long-term credit rating to AA– with a negative outlook – as the structural decline in its letters business has reduced profitability and the current regulatory framework limits its capacity for cost saving measures. Standard & Poor's considers that without material changes to the revenue and cost structure of Australia Post's mail operations, ratings could be further downgraded. A re-consideration of the regulatory framework is now appropriate.

CSOs and Prescribed Performance Standards

The *Australian Postal Corporation (Performance Standards) Regulations 1998* (the Regulations) set out the performance standards (the Prescribed Performance Standards – PPS) to be achieved by Australia Post in meeting its CSOs through minimum standards, including:

- delivery performance (94% of letters on time according to the specified delivery schedule – see **Attachment 1**);
- minimum delivery requirements (98% of delivery points daily and 99.7% of delivery points twice a week);
- a minimum number and locations of retail outlets (4,000 outlets with 2,500 in rural or remote areas); and
- a minimum of 10,000 street posting boxes.

[11] Australia Post Annual Report 2013-14. Australia Post calculates CSO costs on a long run avoided cost methodology. Therefore, these costs are not directly comparable with reserved services profitability figures, which Australia Post prepares on the basis of its full-cost absorption cost allocation model.

[12] The ACCC identified reserved letter services as a potential recipient of a cross-subsidy in 2009–10 on the basis that revenues were less than direct and attributable costs. See p. 13 of *Assessing cross-subsidy in Australia Post 2009–10—An ACCC Report*

[13] Australian and International Postal Services Overview Background Report, BCG

These standards are a major determinant of Australia Post's network structure and operation, including:

- the function and timing of activities;
- the size and location of facilities;
- transport schedules that connect facilities and final delivery points;
- the overall speed and accuracy of the processes; and
- the network resourcing and internal arrangements required to meet the PPS despite significant variation in volumes on a daily and seasonal basis.

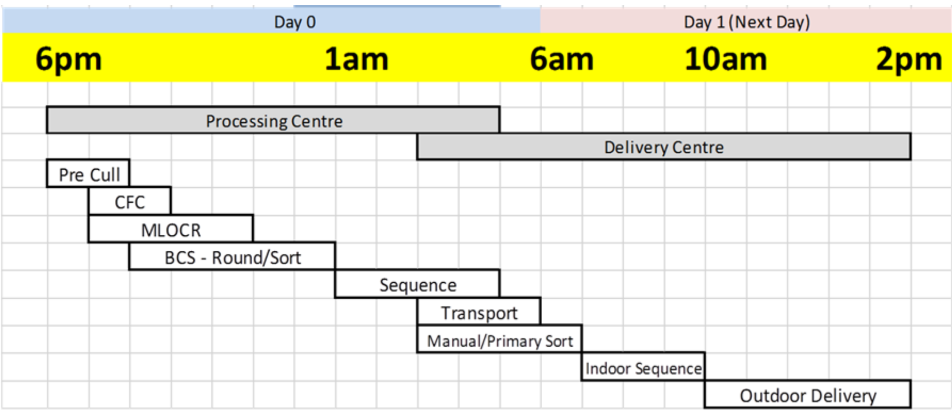
In particular, the strict delivery timeframes require Australia Post to move letters quickly from collection through processing (in the 25 large centres Australia-wide) and out to one of Australia Post's 419 delivery centres. The timing requirements reduce Australia Post's ability to restructure its processing and delivery operations to reduce its reliance on labour, and make it difficult to reduce these costs as letter volumes decline. This is explained more fully in the box below.

Processing and delivery requirements

The large volume of mail still flowing through Australia Post's network, coupled with the strict delivery timeframes, limits the degree of sorting that can be performed in the processing centres – that is, while letters are sorted to individual postal rounds, they are not further sorted into the sequence in which they are delivered by the postal delivery officers.

This sequencing is undertaken once the letters arrive at the delivery centres. Postal delivery officers manually sequence the letters within their rounds, and include large letters and small parcels, prior to the commencement of their delivery rounds. Due to the need to start delivery rounds before around 10am, the manual sequencing starts during a period that attracts penalty rates.

As an example of the time constraints, for the approximately 48% of letters that are delivered in the same city or town, letters collected at 6pm on a given day must be processed and transported to the relevant delivery centre by around 6am the following morning, as shown below:



Culler facer canceller machine (CFC)

Multi-Line Optical Character Reader machine (MLOCR)

Barcode Sorter machine (BCS)

The costs of operating Australia Post's letters network are increasing as the number of delivery points in Australia grows. There are currently 11.3 million delivery points in Australia with the number increasing by around 150,000 per annum[14]. Australia Post has noted that "while addressed letter volumes in 2012-13 were at around the same level as 1994-95, by comparison, the delivery footprint has increased by circa 46%"[15]. **Table 2** below shows the increasing number of delivery points since 2005.

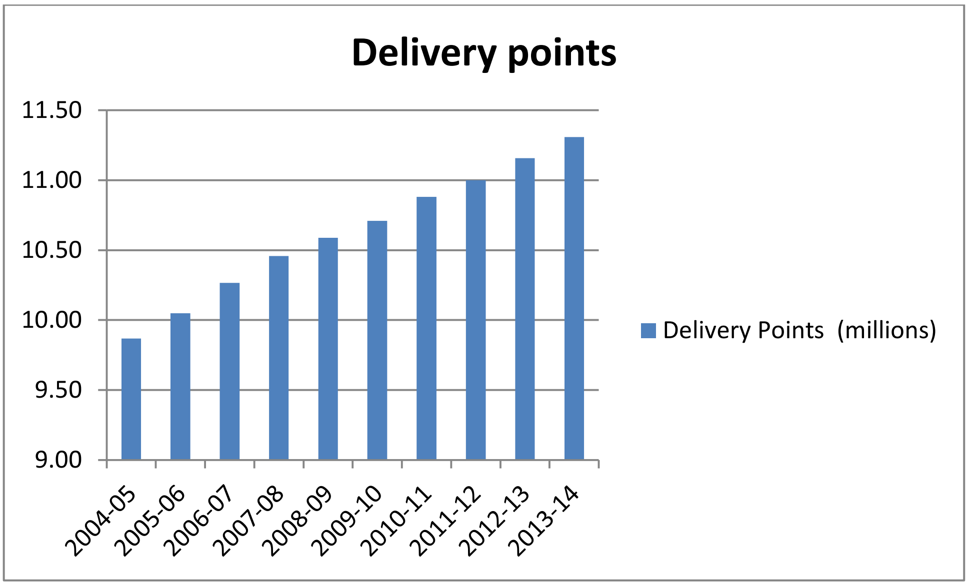


Table 2: Delivery points – increase since 2005

Prices surveillance on the Basic Postage Rate

The ACCC's prices surveillance function is intended to promote efficient pricing and consumer protection where there is reduced competition. Given the complexity of the issues considered by the ACCC and the need to consult with stakeholders, prices surveillance processes can be time-consuming (up to six months) and reduce Australia Post's flexibility to price its products and services appropriately.

However, in a market where there is increased competition from digital alternatives, and Australia Post's letters business is running at a loss, the prices surveillance framework is having the unintended consequence of restricting Australia Post's ability to quickly respond to competitive pressures and the loss of market share by varying the prices it charges for its services.

Measures undertaken to address the challenges

In order to maintain its financial position in the face of declining letter volumes, Australia Post has focussed on reducing labour costs, which are the primary driver of its fixed costs. Australia Post has negotiated an enterprise agreement which has generated productivity improvements and reduced staff levels. Australia Post has also focused on reducing costs through a combination of automation, process redesign and improvements to network systems.

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[14] Australia Post Annual Report 2013-14

[15] *Supporting Statement: Changes to Australia Post's Ordinary Letter Service 31 January 2014*, ACCC.

However, if Australia Post was to undertake the degree of cost reduction required to stem the losses in its letters business, it would not be able to meet the existing CSOs. In considering Australia Post's price notification of 31 January 2014, the ACCC found that "Australia Post's operating costs would need to fall in real terms by around 15% from 2012-13 to 2014-15 in order for domestic reserved services to break even"[16]. Given the degree of efficiency improvements implemented to date, this level of additional cost-cutting would not be possible under the existing CSO requirements.

It is also worth noting that, as revenues from letters services continue to fall because of declining letter volumes, an increased level of cost reduction is required to break even. This is exacerbated by the continuing growth in the letters network as additional addresses are created.

Australia Post has also sought to increase revenues through a range of approaches, including through a $2 billion expansion of its logistics and freight services parcel services. This investment has included the acquisition of StarTrack, a national road freight company.

While these investments have until recently enabled Australia Post to offset losses in letters, its parcels business is under intense competition as retailers with a national footprint and global courier companies enter the domestic parcels market. Australia Post will be undercut on price and service standards as competitors will likely cherry pick profitable routes, with Australia Post required to service a national network as part of its performance obligations.

Australia Post is also expanding the range of government, business and financial trusted services it provides, and has developed the Australia Post Digital MailBox to provide customers with a secure and cost-effective digital channel for connecting with their clients. Australia Post is also establishing Business Hubs, which co-locate Australia Post's transport, delivery and sales expertise to offer operational and service support to small and medium-sized businesses.

The decline in letter volumes being experienced by Australia Post is part of a broader international trend. Many overseas postal service providers have already experienced similar, and in some cases more significant, declines in volumes than those confronted by Australia Post to date. Further detail on the overseas experience, and examples of the policy responses, are at **Attachment 2**.

2. The need for Government action

Australia Post is a GBE, whose activities are governed by Commonwealth legislation and regulation (see **Attachment 1**). While Australia Post has taken action to address the challenges it faces, regulatory reform is necessary to achieve operational efficiencies so that Australia Post can operate a sustainable letters service.

Any government action to address the challenges to Australia Post's declining letters business must consider its Community Service Obligations (CSOs). Australia Post's costs in meeting its CSO have increased over time, totalling $203.5 million in 2013–14[17]. These costs arise where the charges for

[16] *Australia Post price notification for its 'ordinary' letter service, February 2014, ACCC Decision*.

[17] Australia Post Annual Report 2013-14. Australia Post calculates CSO costs on a long run avoided cost methodology. Therefore, these costs are not directly comparable with reserved services profitability figures, which Australia Post prepares on the basis of its full-cost absorption cost allocation model.

mandated services do not recover the costs of providing them – with the cost measured on a net basis after reduction of related revenue.

Section 27 of the APC Act specifies Australia Post's key CSO which requires Australia Post to provide a letter service that is "reasonably accessible to all people in Australia on an equitable basis, wherever they reside or carry on a business." [18] Australia Post undertakes these non-commercial activities to meet the perceived social needs of the community and its international obligations as a member of the Universal Postal Union.

Australia Post is required to provide a letter service for both domestic and international traffic that:

- is reasonably accessible to everyone on an equitable basis;
- operates to performance standards that ensure the service meets the social, industrial and commercial needs of the community; and
- includes a standard letter service at a uniform rate Australia-wide.

In particular, the letter service must be available at a single uniform rate for standard letters carried by ordinary post ('the basic postage rate'). Regulations set the performance standards Australia Post is required to meet in providing this service.

The CSOs recognise the important social and economic role that written communications (in the form of letters) played in Australian society at the time the APC Act was enacted. The postal service represented an important national communications service fundamental to social cohesion and to business and social dealings. At that time, telecommunications services were not an adequate alternative. The CSOs also ensured the availability of and access to affordable postal services throughout Australia, particularly for vulnerable Australians and those living in regional communities.

Since the early 1990s, the evolution of the Internet, mobile services and smart devices has diminished the importance of letter services to the Australian public and business, as evidenced by the decline in letter volumes since 2007–08 and by the growth in online social and business traffic. Notwithstanding this reduction in letter volumes, Australia Post still carried around 3.4 billion addressed letters in 2013–14, which indicates continuing reliance on letters in some sectors of the community, most notably among businesses and governments.

It was originally envisaged that profits from reserved services would be sufficient to fund CSO costs. However, since 2008–09, Australia Post's domestic reserved letter service has operated at a loss. Given that Australia Post must deliver its CSO regardless of whether there is sufficient profit to fund the CSOs, this cost has been met from Australia Post's non-reserved mail business and other commercial activities[19]. However, these profits are no longer sufficient to cover losses in the letters business.

[18] See Division 1 of Part 3 of the *Australian Postal Corporation Act 1989* (APC Act)

[19] The ACCC identified reserved letter services as a potential recipient of a cross-subsidy in 2009–10 on the basis that revenues were less than direct and attributable costs. See p. 13 of *Assessing cross-subsidy in Australia Post 2009–10—An ACCC Report*

The question arises as to whether the basic mail service is a 'public good'. While the service may have some elements of a public good, it also contains characteristics which prevent it from being classified as such. A public good is both non-excludable (that is, individuals cannot be excluded from consumption) and non-rivalrous (ie, usage by one individual does not reduce availability to others). Consumption of the letter service is restricted to those willing to purchase the service, effectively excluding those consumers who are not willing to play. Furthermore, the major benefits of the basic mail service are captured by direct participants in the transaction (the sender and the recipient).

The Australian Government could provide funding to support Australia Post's letters business. However, this would not address the fundamental structural issue of declining letter volumes and could reduce incentives for Australia Post to provide an efficient letters service while delivering no productivity benefit to society. It would have an ongoing significant Budget impact due to the large and increasing cumulative losses forecast in the letters business ($3.6 billion over the period 2014-15 to 2017-18) and, in the absence of regulatory reform, the funding would simply be a subsidy from taxpayers to the employees and customers (the majority of which are businesses and government agencies) of Australia Post.

This measure would also be inconsistent with the APC Act and the Australian Government's GBE policy which require GBEs to add to their shareholder value by operating efficiently, pricing efficiently and earning at least a commercial rate of return. An effective and timely response to Australia Post's immediate financial viability issues involves urgent revision of outdated regulatory requirements. This will enable Australia Post to increase revenue and generate productivity improvements leading to reduced operational costs. It is also consistent with the Government's deregulation policy agenda.

3. Policy options

The objective of any policy response by the Australian Government would be to modernise the postal regulatory framework in a way that reflects the fundamental changes in the postal market, and enables Australia Post to deliver a sustainable letter service.

The following options are considered:

1. Retention of the current regulatory arrangements – i.e. maintain the status quo;
2. Deregulation of the letters market – i.e. remove pricing oversight (including Ministerial disapproval of price increases) and Australia Post's letters monopoly; and
3. Reform of the postal regulatory framework, which includes reform to regulatory measures.

The Australian Government has stated that it will not privatise Australia Post.

1. Retention of current regulatory arrangements

Under this option, Australia Post would continue to supply a postal service with no reform to its regulatory framework. Given the ongoing losses in the letters business, Australia Post's options to continue to provide the postal service in a sustainable manner would be limited. They include seeking to further reform its operations to gain additional efficiencies, increasing revenues through postage rate increases or obtaining additional funding.

Australia Post has made considerable efforts to modernise its operations, including its Future Ready program of corporate reform. Given these efforts and without reform to the regulatory framework, Australia Post would have had to reduce its workforce to realise operational efficiencies. This would have serious consequences on its ability to deliver its community service obligations.

Australia Post may seek to increase its revenues through further rises in the BPR. However, these increases would need to be significant as they would be coupled with the current performance standards. Furthermore, if allowed, such increases would contribute to letter volumes declining more quickly as customers sought more cost-effective alternatives. This could lead to a 'vicious circle' of rising postage prices and increased rates of volume declines, further exacerbating Australia Post's financial position.

Australia Post could also seek to further diversify its business operations, but may find it difficult to source the required capital to fund major acquisitions outside of its core operations. It would have to rely on building capacity and expertise which takes years to develop placing the organisation at a competitive disadvantage. Depending on the proposed activity, Australia Post may also be limited by section 14 of the APC Act, which states that Australia Post's principal function is to "supply postal services within Australia and between Australia and places outside Australia".

2. Deregulation of the letters market

The domestic letters market could be opened to full competition by revoking the pricing oversight arrangements and removing Australia Post's letters monopoly, thereby allowing other parties to collect, carry and deliver letters. This would be accomplished by:

- amending the APC Act to allow other parties to collect and deliver letters – including removing the requirement that they charge at least four times the BPR to do so; and
- removing price controls over the delivery of letters by removing the ACCC's pricing oversight role and the Minister for Communications' power to disapprove increases in the BPR.

This would involve significant revision of the APC Act and other regulatory changes[20].

3. Reform of the postal regulatory framework

This option recognises that there remains a legitimate ongoing need for a postal service and that appropriate regulatory reform would enable Australia Post to modify its operations to meet the challenges arising from letter volume declines. It involves amending some of the regulations governing Australia Post's performance and market behaviour – specifically to:

(i) enable Australia Post to offer new letters services for all reserved letters; and
(ii) reduce or remove pricing constraints on these letters services.

The objective of the proposed reforms is to provide Australia Post with greater flexibility to adjust its letters services and the prices it charges. The reforms would enable Australia Post to improve its short-term financial viability by:

- introducing new letter products with different speed parameters;
- better aligning the prices it charges for these postal services with the costs of delivery; and

[20] It is not proposed that the reforms would include revoking the prescribed performance standards

- restructuring its letter processing and delivery operations to realise efficiency gains.

Australia Post can already implement the first element to a limited extent. Two-speed services for PreSort Letter and Charity Mail have existed for well over a decade and were introduced for Clean Mail, Imprint Mail and Metered Mail from June 2014. However, the $0.70 BPR sets a ceiling on prices Australia Post can charge, and there is limited pricing "headroom" for Australia Post to introduce a level of price differentiation under which customers may choose to switch to the lower priced service. For example, an off-peak ordinary letter service at $0.65 provides little incentive for letter customers to amend operations if the BPR is set at $0.70.

In relation to the second element, Australia Post already has the power to introduce premium services and price them at a level greater than ordinary letter rates. For example, letters can be sent through Australia Post's Express Post service. However, prices (which commence at $5.75) are considerably higher than those for the letters service. In addition, because the PPS already require next day delivery of ordinary letters in metropolitan areas there is little or no scope to introduce a letters service that represents a premium to this existing standard.

It is the combination of the existing PPS and prices oversight that limits Australia Post's ability to respond to changing market conditions by either increasing the price it charges for its services, or by reducing the frequency and / or speed of delivery.

The specific proposed reform measures are described below.

(i) Amendment of the PPS

As noted above, Australia Post must meet the performance standards set out in the PPS, including in relation to the frequency, speed and accuracy of mail delivery. These requirements impose a high fixed cost burden (estimated at 80% of costs[21]) on Australia Post, arising from the need to carry out a significant part of letters processing overnight and to maintain a delivery network that covers all the (current) 11.3 million delivery points in Australia. Relaxation of the performance standards would enable Australia Post to modify its letter processing and delivery operations to more easily reduce costs in line with declining letter volumes.

If regulatory changes are made to enable Australia Post to offer two-speed letter services for all reserved letters, Australia Post has indicated that it would introduce a more expensive Priority letters service and a cheaper Regular letters service.

Australia Post will still be required under Regulation to provide a daily letter service, excluding weekends and public holidays, to 98% of delivery points.

Over time, Australia Post expects consumers to choose to switch to the Regular service allowing Australia Post to achieve cost savings through operational and workforce changes related to the altered delivery schedules.

Under the existing two-speed bulk mail service, the PPS apply to the Priority service. If regulatory changes are made to enable wider introduction of two-speed services, a decision must be made as

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[21] *Australian and International Postal Services Overview Background Report*, BCG

to which letters service is the 'ordinary post' for the purposes of postal regulation. That is, which service provides the CSO – the Regular or Priority service?

The Regular letters service as the 'ordinary post'

Under this scenario, the PPS could be amended to enable Australia Post to deliver Regular letters less frequently and slower. This service would still be a universal service, with mail being delivered to all delivery points in Australia.

The Priority letters service as the 'ordinary post'

The designation of the Priority service as the ordinary post has the potential to impact Australia Post's competitors, particularly if Australia Post is given greater pricing freedom over this service. Other service providers are prohibited by sub-section 30(1)(e) of the APC Act from carrying standard letters for less than four times the BPR. If Australia Post was to increase the BPR significantly (e.g. to $1.50) then this would require competitors to charge (in this example) at least $6.00 to carry and deliver a similar article.

Designation of the Priority service as the ordinary post would also not be in line with changing community expectations of the postal service.

(ii) Reduce or remove ACCC pricing oversight

On the assumption that regulatory reforms to enable the introduction of the two-speed letters service (as described above) are implemented, there are a range of possible approaches to amend the pricing oversight arrangements for each of the two letters services:

3(a) **Priority** and **Regular** letters – retain ACCC pricing oversight for both services

3(b) **Priority** letters – light regulatory arrangement – e.g. price monitoring and Minister/Treasurer has power to refer Australia Post's prices to the ACCC
Regular letters – retain full ACCC pricing oversight arrangements

3(c) **Priority** letters – no ACCC/Ministerial pricing oversight
Regular letters – retain full ACCC pricing oversight arrangements

3(d) **Priority** letters – no ACCC oversight or light touch regulatory arrangements
Regular letters – light touch regulatory arrangements

These options are summarised below.

Option	Letter service	ACCC pricing oversight	Ministerial s.33 power to disapprove
3(a)	Priority	Yes	Yes
	Regular	Yes	Yes
3(b)	Priority	No	Yes (and possible referral to the ACCC)
	Regular	Yes	Yes
3(c)	Priority	No	No
	Regular	Yes	Yes

Option	Letter service	ACCC pricing oversight	Ministerial s.33 power to disapprove
3(d)	Priority	No	No
	Regular	No	Yes (and possible referral to the ACCC)

Table 3: Pricing oversight reform options

Australia Post's letters monopoly is not affected by these regulatory changes, and the ACCC would retain its existing responsibilities for:

- monitoring for any cross-subsidy from Australia Post's reserved service to its non-reserved commercial activities; and
- inquiring into disputes regarding the bulk-mail services.

4. Impact analysis

Each of the options directly impact Australia Post and the Commonwealth as they remove, to varying degrees, administrative costs while providing Australia Post with increased flexibility to alter its prices and product offerings.

The impact on stakeholders of any changes that Australia Post may make will depend on the willingness and ability of customers to mitigate the impacts – for example by moving letter volumes from the Priority to the Regular service, or by transitioning away from letters to alternative digital communications channels.

The analysis below outlines the expected impacts from the proposed implementation of:

- Option 2 – deregulation of the letters market
- Option 3 – reform of the postal regulatory framework, including regulatory changes to enable:
  - two-speed letter services; and
  - reform of the pricing oversight arrangements.

Key stakeholders

The important role that Australia Post plays in the economy and the daily lives of consumers means that, even though the importance of this role is declining, any reforms to the postal service will be felt across the community. The impact analysis below considers the effects of the proposed reforms on Australia Post itself as well as on its key stakeholders, including:

- The Australian Government – as owner and shareholder
- Retail outlets – including LPOs
- Australia Post's workforce
- Senders of mail – including all levels of government, businesses and individuals, mail houses and the printing industry
- Regional communities
- Vulnerable groups – e.g. the elderly, those who cannot easily access the Internet (because of cost, lack of services, etc.)
- The Australian postal industry
- The broader Australian economy.

Option 2 – Deregulation of the letters market

Deregulation of the letters market – impact on Australia Post

Competition

Under Section 29 of the APC Act, Australia Post has a statutory monopoly to collect, carry and deliver standard letters within Australia.

If the letters market was deregulated, Deloitte Access Economics[22] suggests that competition could enter the Australian market at around $3.00 to ensure a sufficient return on investment. However, this price is relatively high compared to Australia Post's current stamp price of $0.70. There are also high barriers to entry for new competitors seeking to establish competing mail networks. These include high upfront investment, network size, the need to interconnect with other postal networks, Australia Post's established brand name and reputation for reliable service and the regulatory uncertainty. Australia Post's current network, which connects all Australian households and businesses, offers a significant competitive advantage as it is able to provide an end to end domestic letter service. The letters market is also declining rapidly (with estimated future letter volume declines of 8% – 11% per annum) and this would be a key factor in determining whether any competitor would enter such a market.

Overall, it seems quite plausible that if the letters market was significantly deregulated, the extent to which competing networks would be set up in competition with Australia Post would be limited. It is moderately likely is that competitors would "cherry pick" particular market segments, only offering services in low cost, high revenue areas (e.g. large metropolitan centres with links to similar areas in other states/territories) where the probability of returning a profit is higher. This is what has occurred in the deregulated business areas where Australia Post is competing, particularly its parcels business.

International experience supports this conclusion. Competition in the postal markets has been introduced in a number of countries since the early 1990s, particularly in Europe. Competition has grown slowly and, in those countries where postal markets have been opened to competition for the longest period of time, the total level of competition is still relatively small compared to the incumbent USP. For example, the Finnish and Swedish postal service providers have each retained approximately 85% market share despite competition since the early 1990s[23].

There are two countries (Germany and the Netherlands) where competitors have gained larger market share (over 10%). However, these countries are considered exceptions and the market share includes non-standard letter items such as advertising mail. Competition in correspondence mail is very limited with competitors focussing on small geographic areas and mail routes in high population densities[24].

[22] Deloitte report, p.59
[23] Deloitte report, p.52
[24] Deloitte report, p.53

A deregulated market with competitors focussing on specific geographic areas would provide scope for suppliers to develop new and more innovative services or provide the same service as Australia Post at a lower cost. This competition would in turn place greater pressure on Australia Post to further contain its costs and improve service quality and product diversity.

As part of its CSO, Australia Post would have an ongoing obligation to service all areas of Australia. With reduced revenue from the more profitable areas, Australia Post would have diminished capacity to cross-subsidise higher-cost elements of its letters network (including regional, rural and remote areas). In view of Australia Post's current and forecasted financial losses, such an outcome would further exacerbate Australia Post's deteriorating financial position. Australia Post's modelling shows that introducing competition to the Priority letters service could result in a cumulative enterprise loss of $182 million from 2014–15 to 2017–18. With deregulation, this financial impact is likely to be more substantial.

Australia Post may also need to increase prices of its letters services to offset losses in its letters business.

It would most likely lead to Australia Post requiring a funding injection (e.g. through asset divestment, debt funding or an approach to the Australian Government) in the medium term to enable it to continue to provide the CSO.

Pricing oversight

If the current pricing constraints on Australia Post (i.e. ACCC pricing oversight and Ministerial power to disapprove price increases) are removed, Australia Post would have greater freedom to increase the prices of its letters services. While giving Australia Post greater ability to respond to market changes with revised product pricing, this approach has several possible outcomes:

- while raising prices may enable Australia Post to increase revenues (at least in the short term), it may increase scope for competitors to gain market share through lower-price product offerings (i.e. by undercutting Australia Post's prices); and
- Australia Post may choose to rely more heavily on price increases to address its financial situation. This is more likely if Australia Post faces strong resistance to any proposed operational and service changes from its workforce and the broader community.

Deregulation of the letters market – impact on stakeholders

The Australian Government

If the losses projected by Australia Post are realised, it would increase the urgency for further reform, and may contribute to a need for government funding assistance to enable Australia Post to continue to provide the letters service. The level of support required is likely to be significantly higher than in the 'no reform' option, as the expected introduction of competition in low-cost areas would result in considerable revenue reduction for Australia Post.

The option exists to require new market entrants to contribute to the CSO cost. While this may reduce the CSO cost to Australia Post (and potentially the Commonwealth), it could also reduce the attractiveness of the market for potential competitors and limit the benefits arising from increased competition.

The introduction of competition at this time is problematic where letter volumes are declining and Australia Post's letter business is incurring substantial and increasing losses. This option may also limit the options available for future comprehensive reform.

Retail outlets – including LPOs

There is no proposal to amend or remove the requirement for Australia Post to maintain a network of at least 4,000 retail outlets and Australia Post has committed to maintaining its extensive post office network, recognising the critical role its network plays in regional communities. As such, the proposed deregulation is not expected to directly impact the retail network.

Australia Post's workforce

If the losses projected by Australia Post are realised and funding support is not available (through either industry-based CSO contributions or direct funding), Australia Post would need to implement further operational efficiencies where possible, 'downsize' by divesting non-postal business units and/or reduce staffing levels. This would have a significant negative impact on Australia Post's workforce and, in the event that Australia Post was forced to cease providing services, would result in the loss of all remaining jobs.

Senders of mail

If competition arises, letter senders are likely to benefit through greater choice of providers – though this may be limited to letters sent to metropolitan areas.

Cherry picking of profitable mail routes would result in increasing financial pressure on Australia Post and its delivery of the CSO.

Senders using Australia Post for all or part of their letter service are likely to face increased postage costs as it attempts to compensate for any loss of revenue in more profitable areas. This would increase the costs of letters sent to areas not serviced by Australia Post's competitors.

It is not clear that competition would increase productive efficiency and, indeed, may decrease it as a consequence of increased prices for end users. Postal operations for letters have strong monopoly characteristics and international experience suggests it is not possible to economically duplicate parallel postal operations. If attempted, the postal operators would either struggle financially (and may fail) or would have to raise prices – neither of which benefits end users. Furthermore, if cherry picking of high value areas does arise, there would need to be a CSO levy imposed on those cherry picking in order to have some degree of regulatory neutrality.

Regional communities

To the extent that Australia Post is required to deliver the CSO, and is financially able to do so, there is expected to be limited impact on letter senders and consumers in regional Australia.

However, if Australia Post's financial situation deteriorates to the point that it can no longer provide a letter service, it is unlikely that any competitor will offer a general service to regional areas.

Vulnerable groups

Vulnerable groups may have greater choice of providers for letters sent to/from metropolitan areas.

To mitigate the impact of stamp price increases for vulnerable Australians, Australia Post recently introduced its MyPost Concession Account. This account entitles approximately 5.7 million

Australian concession card holders to receive five free stamps initially, and to be able to purchase up to 50 discounted stamps (priced at $0.60) annually. Australia Post has committed to maintain this concession rate and will continue to offer all Australians $0.65 stamps for Christmas cards, which account for the bulk of social mail each year.

Australian postal industry

This option is likely to provide increased opportunities for existing courier/parcel companies to broaden the range of services they provide in the postal sector, and for new entrants to offer services in Australia. As noted, it is not considered likely that they would offer services in regional, rural and remote areas of Australia.

There may be a requirement for new letter market entrants to contribute to the cost of the CSO.

Broader Australian economy

Overseas experience suggests that any competition arising from the deregulation of the letters market is likely to be limited. The introduction of competition has been a feature of a number of overseas postal reforms – in particular as a result of European Commission initiatives.

Competition has grown slowly in European countries with the overall level of competition still relatively small. For example, the Finnish and Swedish postal service providers each have retained approximately 85% market share despite competition since the early 1990s[25].

If deregulation does result in increased competition in the delivery of letters, this would be expected to result in lower prices and/or an improved range of services in areas which are likely to be profitable for new entrants – i.e. high population, metropolitan areas. Other areas may incur increased postage costs as Australia Post raises prices in an effort to mitigate the losses arising from competition.

Discussion

Deregulation of the letters market is expected to offer benefits to new letter service providers entering the market, and some senders of letters – particularly in relation to letters sent between metropolitan areas.

However deregulation, and particularly the introduction of competition, is likely to have a significant negative financial impact on Australia Post. If realised, this could lead to either the need for a significant funding injection or Australia Post divesting assets and businesses not required to deliver the letters CSO. Without funding support, Australia Post will eventually reach a point where it can no longer trade and would cease providing services, with a major impact on the letters market and the economy generally.

It is also worth noting that, while there is no direct competitor in the regulated letter market, Australia Post still has an incentive to be efficient. The loss-making nature of the CSO, and the need for Australia Post to cross-subsidise the loss-making elements of the letters business from the profitable elements as well as from the competitive segments of the business, gives Australia Post significant incentive to operate the letters network as efficiently as possible.

[25] Deloitte report, p.52

Overall, implementation of this option is expected to result in a **net negative** impact.

Option 3 – Reform of the postal regulatory framework

Implementation of two-speed letter services

The proposed reform to the performance standards is to allow Australia Post to introduce two-speed letter services.

Two-speed letter services – impact on Australia Post

The proposed reforms to implement two-speed letter services would increase (on average by a maximum of 2 days) the time available to Australia Post to process, transport and deliver Regular letters. This would have several key impacts that would enable Australia Post to introduce operational efficiencies and reduce costs as letter volumes decline:

- more of the letter processing can be done during the day, reducing the overall number of employees required and the need for overnight processing;
- an increased level of sorting (to delivery sequence within each round) could occur in the processing centre, reducing the need for postal delivery officers to manually sequence letters during particular periods; and
- Australia Post would invest in additional specialised sorting machines to facilitate the more intensive level of sorting in the processing centres.

Two-speed letter services – impact on stakeholders

The Australian Government

Improved financial outcomes for Australia Post would result in reduced risk to the Federal Budget.

Retail outlets – including LPOs

There is expected to be little or no impact on retail outlets.

Australia Post's workforce

The proposed operational changes will impact on Australia Post's workforce, primarily the processing and delivery staff. Australia Post has developed its 'Post People 1st' strategy to assist the workforce transition through the reform process. This strategy will:

- provide financial and retirement planning to employees electing to retire or take a voluntary redundancy;
- increase the visibility of job vacancies to support redeployment within Australia Post;
- improve access to education and training services; and
- provide career support and information.

Australia Post is committed to retraining and redeploying all of its employees, and will not force redundancy on any employee directly affected by postal reform. Headcount reductions in the letters business will be managed through natural attrition and by redeploying employees to growth areas like parcels as part of Australia Post's 'Post People 1st' Program.

Senders of mail

Senders will have a choice of letter services – either the more expensive, high-speed Priority service or the cheaper but slower Regular service. It is expected that, consistent with Australia Post's experience in the two-speed business service (which was extended in June 2014) the majority of senders will use the Regular service. Since the expansion of the service, a significant volume of mail has migrated to the Regular letters service, with around 70% of eligible mail now being sent through that service[26].

Regional communities

Consumers in regional Australia would be affected to the extent that the speed standards relating to letter delivery in regional areas are amended. The slowest delivery speeds currently defined under the performance standards are for deliveries between:

- non-metropolitan and metropolitan areas in different states – at D+3; and
- non-metropolitan areas in different states – at D+4.

Under the new delivery speeds, letters would be delivered 1-2 days slower for mail in the same state and 1-3 days slower for interstate mail. Overall, around 66% of letters would be delivered within 2-4 days of sending. See Table 4 below for more details.

Table 4: Proposed Priority and Regular delivery time frames

			Business Letters	
	% of total letters	**Current Timetable (per PPS)**	**Priority Timetable**	**Regular Timetable**
Within same state	**65.7%**			
Within same city, town or metro area	48.1%	1	1	2-3
between metro and country areas	13.4%	2	2	3-4
between country areas	4.1%	2	2	3-4
Between States	**34.3%**			
between capital cities	21.4%	2	2	3-5
between capital cities and country areas	11.7%	3	3	4-6
between country areas	1.2%	4	4	5-7

Vulnerable groups

Many mail recipients may receive mail a little slower (i.e. one or two days). In most cases, this is not expected to be a problem (Deloitte has noted that "there is little empirical evidence to suggest that vulnerable groups value delivery speeds higher than other groups"[27]). Where a quick response is necessary, mail senders may need to adjust processes to send letters earlier, utilise the Priority service or use a digital alternative (such as email).

[26] The price differential between the Regular and Priority services for small letters varies from $0.03 to $0.074 depending on the category, weight and destination of the mail

[27] Deloitte report, p.v

Australian postal industry

There is expected to be little or no impact.

Broader Australian economy

Two-speed letter services (Regular and Priority services) are already available for some categories of business mail. Australia Post introduced Regular and Priority letter services for PreSort Letter and Charity Mail over a decade ago and extended this to Clean Mail, Imprint Mail, Metered Mail and Local Country letters in June 2014. Around 85% of Australia Post's letter volumes are currently delivered under these letter categories.

Letters sent using the Regular service are delivered 1-2 business days slower than Priority letters and the price differential between the two services (for small letters) varies from $0.03 to $0.074 depending on the letter category and the posting and delivery destinations.

The extension of the service has been accepted by the business community and, since the extension, around 70% of eligible mail has migrated to the Regular service (equating to around 60% of total letter volumes).

The proposed extension of two-speed letter services to the remainder of letters, including social mail, is expected to have a similar impact.

Discussion

The implementation of two-speed letter services across all reserved services is expected to impact on Australia Post's processing and delivery workforce.

Overall, the reform offers a **net benefit** with:

- financial benefits for Australia Post, enabling improvement of its financial position through more efficient and sustainable provision of the letters service;
- impacts on Australia Post's processing and delivery workforce; and
- no significant impact on other stakeholders.

Implementation of pricing reform

Australia Post has indicated that the cost savings identified above are unlikely to be sufficient to return the letter service to profitability and that "instead, relatively large increases in revenue will be needed, requiring higher prices"[28]. Australia Post has advised that, in the event that reforms are implemented to enable it to expand its current two-speed letter service to cover all letters, it would increase the postage rate for both services.

The analysis below considers the likely impacts arising from implementation of the pricing oversight reform options listed above and is based on the assumption that the regulatory changes to allow two-speed letters are agreed.

[28] Deloitte report, p.vii

Pricing reform – impact on Australia Post

Options 3(c) and 3(d) (see Table 3) offer the greatest potential benefit for Australia Post, as they provide freedom to increase prices for the Priority service (i.e. without ACCC or Ministerial oversight). The impacts for each option are summarised below in Table 5.

3(a)	The current process to increase prices will apply to both the Priority and Regular letters service, and Australia Post would have to lodge a price notification with the ACCC and advise the Minister for Communications of proposed price increases in either service. The current process delays and pricing uncertainty will continue – limiting Australia Post's ability to increase prices of each service. Under the ACCC's assessment process, prices for the Regular service would be limited to those that reflect an efficient cost of providing the service plus a reasonable return on capital, as assessed by the ACCC. The ACCC may endorse greater price increases for the Priority service to reflect the higher cost of providing this faster service.
3(b)	Australia Post would not have to lodge a price notification with the ACCC for the Priority service, but would still be required to advise the Minister of its intention to increase prices for both services. In making a decision on whether to disapprove the proposed increase, the Minister would have the ability to request expert advice, possibly from the ACCC. Australia Post would still be required to lodge a price notification with the ACCC for the Regular service, meaning that it would not avoid the time delays inherent in the ACCC's assessment process. Under this option, Australia Post may have an improved ability to increase prices for the Priority service, but current process to obtain price increases for the Regular service would continue.
3(c)	Australia Post would not have to lodge a price notification with the ACCC for the Priority service, but would still be required to do so for the Regular service and so would not avoid the time delays inherent in the ACCC's assessment process. Australia Post would have an improved ability to increase prices for the Priority service, but the current process to obtain price increases for the Regular service would continue.
3(d)	Australia Post would not have to lodge a price notification with the ACCC for either the Priority or Regular service. Australia Post would still have to notify the Minister for Communications of its intention to increase prices for the Regular service and the Minister would have the power to disapprove any such increase. Under this option, Australia Post would have an improved ability to increase prices for the Regular service, subject to Ministerial disapproval.

NOTE: Modelling on the financial impacts on Australia Post of letter pricing changes involves commercial-in-confidence information and has been redacted

Table 5: Pricing reform – impact on Australia Post

Pricing reform – impact on stakeholders

The Australian Government

The Australian Government has an interest in Australia Post from financial, policy and regulatory viewpoints to:

- enable Australia Post to continue to operate in a sustainable manner, and not present a risk to the Federal Budget;
- ensure that Australia Post continues to provide a service that meets the social, industrial and commercial needs of the community; and
- ensure that Australia Post continues to meet its legislative and regulatory obligations.

As a GBE, Australia Post is 100% owned by the Australian Government, and Australia Post's performance is already having a financial impact on the government. As a result of the decline in letter volumes, Australia Post has advised that it does not expect to provide dividends to the Australian Government in the future.

If Australia Post cannot remain financially viable, there may be pressure for the government to provide Australia Post with a capital injection to enable it to continue to provide the CSO. This would present a risk to the Federal Budget, especially as (in the absence of regulatory reform) Australia Post has projected significant operating losses over the period to 2017–18.

As discussed above, while price (and hence revenue) increases are possible under Options 3(a) and 3(b), Options 3(c) and 3(d) offer the greatest potential for Australia Post to increase prices, particularly for the Priority service. As such it is most likely to increase Australia Post's revenue and its enterprise bottom line, and thereby reduce the financial risk to the Australian Government.

Retail outlets – including LPOs

Australia Post is required to maintain a number of postal outlets (see Table 6 below), and it currently exceeds these requirements.

	Total retail outlets	Retail outlets in rural or remote zones
Australia Post requirement	4,000	At least 50% of all retail outlets and, in any event, not fewer than 2,500
Actual numbers (Source: Australia Post 2014 Annual Report)	4,417 retail outlets, comprising: • 740 corporate outlets; • 2,915 LPOs; and • 762 community postal agencies.	2,560 (58%)

Table 6: **Number of Australia Post retail outlets**

There would be no impact under these reforms on Australia Post's current requirements relating to the numbers and locations of retail outlets.

The BPR influences many of the payments that Australia Post makes to LPOs. For example, of the $324 million that was paid to licensees in 2012–13, approximately $200 million was linked in some form to the BPR (many payments are not tied to letter volumes however). The $0.10 increase in the BPR in March 2014 is contributing to a $25 million increase in payments to LPOs in 2014–15. If the

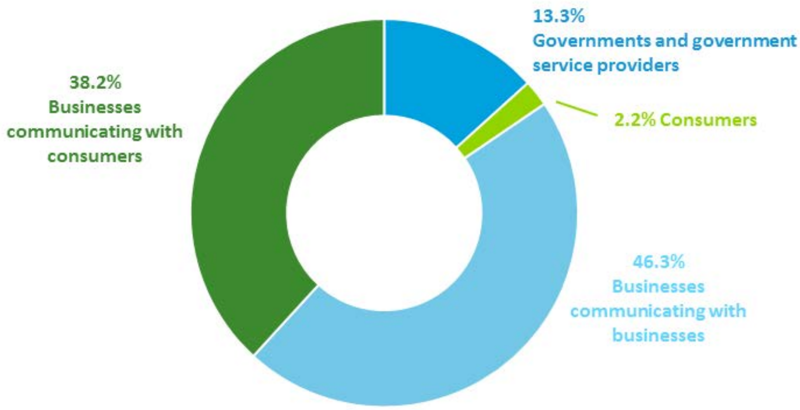
BPR increases to $1.00, Australia Post could deliver on average an extra $20,000 per annum to each LPO, significantly improving the viability of the LPO network.

Australia Post's workforce

There is expected to be little or no impact on Australia Post's workforce arising from the proposed pricing reforms.

Senders of mail

The majority of mail is currently sent by businesses and the three levels of government, with only around 3% of mail being social mail (i.e. consumer to consumer). Around 74% of mail is transactional (e.g. bills), while the remaining 23% is promotional mail. A breakdown of the postal market is shown in Chart 1 below.



Source: IBISWorld

Chart 1: Australian postal market segmentation (2013–14)

As postage rates increase, Australia Post's customers will incur additional costs to send mail. The price impact under each option will depend on their ability to send mail by the cheaper Regular service. Deloitte has noted that "while both senders and receivers will share the costs of the reduced delivery speeds, it will predominantly be businesses and government bearing the financial costs of price rises"[29].

Price increases will likely lead to customers choosing to switch to the lower priced Regular service. This scenario is most likely to occur under Options 3(c) and 3(d). As noted above, a significant number of customers have switched to Australia Post's bulk mail Regular service since its introduction in June 2014.

Irrespective of any increase in postage rate, people are already moving to digital alternatives because of the ubiquity, convenience, and cost effectiveness of digital channels. For example, financial institutions are encouraging customers to access monthly statements online by levying a

[29] Deloitte report, p.37

fee for issuing paper statements. In addition, the Government established the DTO not only to make government more accessible and responsive, but also to improve the quality and availability of digital services.

Regional communities

Australia Post estimates that around 10% of all letters originate from regional Australia in 2012–13 – including around 29% of stamped letters and 7% of business letters. Increases in letter prices will have a similar impact on letter senders in regional areas as on those in metropolitan areas.

Vulnerable groups

This includes elderly Australians and the economically disadvantaged who may have reduced capacity to absorb additional postal costs – vulnerable groups can also include those in rural and remote areas that may have limited or no access to online services.

Australia Post has committed to maintain the MyPost Concession rate at $0.60. The Christmas rate stamp at $0.65 will continue to be offered to all Australians, given that this is when the bulk volume of social mail is sent.

In addition to the potential cost impacts, consumers will also receive mail slower . There is not expected to be significant community concern at this outcome. It is expected that businesses requiring responses from their customers in a certain timeframe will either utilise the Priority service or adjust their processes.

Australian postal industry

As noted earlier, there are limits on the ability of other parties to compete with Australia Post in the delivery of letters. In particular, no other party can carry / deliver a letter for a fee or charge less than 4 times the BPR. As this rate is currently $0.70, the lowest another party can charge to deliver a letter (i.e. the "floor price") is currently $2.80, however this can be expected to increase as the BPR rises over time.

Depending on the prices charged by Australia Post for the Priority and Regular services, and the levels of discount it offers under each service, there may be additional opportunities for mail houses to provide aggregating services for major business and government senders of letters.

Broader Australian economy

There is a diminishing reliance on the postal network to meet the communications needs of Australian individuals, business and governments. Social mail has been largely replaced by digital alternatives and, though business and government letter volumes are still significant, they are also being replaced by increasingly sophisticated and efficient digital channels – e.g. online transactions. Nevertheless, it is important for Australia Post to continue to provide postal service while the need for letter delivery remains, and it is essential that Australia Post provide the service as sustainably as possible.

Interaction between governments, businesses and individuals using digital technology is more efficient and cost-effective than through other forms of communication and transaction (such as letters). An increased level of digital substitution, driven in part by increased postage costs, would contribute to improved efficiency across the economy. Options 3(c) and 3(d) are the most likely scenarios to provide letter senders with additional encouragement to switch to digital alternatives and realise these economic benefits.

Discussion

Options 3(a) – 3(d) respectively give increasing degrees of freedom to Australia Post to raise the price of its letter services. Increased prices would likely lead to customers choosing to switch to the cheaper Regular service, which would allow Australia Post to realise operational cost savings and increase revenue.

At the same time, these options place increasing costs on Australia Post's customers and other stakeholders. In addition, the speed at which prices increase will significantly affect the impacts on the various stakeholders arising from the reform process.

An increased speed in the number of customers choosing to switch to the Regular service also hastens the time at which operational changes can be made which will have a significant impact on Australia Post's processing and delivery workforce. Australia Post will maintain its commitment to retraining and redeploying employees, and will not force redundancy on any employee directly affected by any operational change.

Overall, Option 3(c) is considered to offer the **highest net benefit** of the four options considered.

This option provides a balance between Australia Post's ability to increase prices (and hence revenue) and protection for consumers from excessive price increases, through continued ACCC oversight of the Regular letter service. It offers Australia Post greater freedom to increase prices, particularly on the Priority service, than options 3(a) and 3(b), while maintaining a strong community service obligation on the Regular service and ensuring that all Australians continue to have reasonable access to the letters service. This option will enable Australia Post to more quickly implement the operational changes required to improve financial sustainability. While option 3(d) offers greater pricing freedom, it also reduces ACCC scrutiny on the price of the 'safety net' Regular service.

The impacts on the community are mitigated through continued Australian Government oversight of the Regular service. While postage rates are expected to increase under all options, ACCC review will ensure that the price of the Regular service is limited to a level that will meet the efficient cost of delivering the service, as well as a reasonable rate of return. While there would be no regulatory oversight on the Priority service, this is a 'premium' service, and customers have the ability to use the Regular service instead.

Regulatory burden measurement and cost offset estimate

The regulatory reforms will allow Australia Post to implement operational efficiencies associated with processing, transport and delivery of letters, and realise average annual regulatory cost savings of $211.8 million.

The methodology to determine the regulatory cost savings was agreed with the Office of Best Practice Regulation. There are no regulatory costs on businesses, community organisations or individuals, and no offsets are required.

The information underpinning the determination of the regulatory cost savings is commercial-in-confidence and has been redacted.

5. Consultation

Consultation undertaken

Prior to consideration of the reform options by the Australian Government, Australia Post consulted stakeholders on the challenges facing Australia Post as well as the reform options and their possible impacts. Australia Post's consultations encompassed:

- community engagement events –including face-to-face discussions, Listening Posts, community discussion groups, and roundtable meetings with local community leaders. As at the end of March 2015, 141 community engagement events were conducted across all states;
- discussions with small business, licensees, Australia Post's workforce and trade unions;
- a *National Conversations Portal* which attracted over 100,000 visitors and received a 35% response rate (for example, posting views, voting on polls, etc.);
- a *Workforce Conversation Portal* where employees could post comments or ask specific questions about Australia Post's circumstances and reform options;
- customer surveys on possible change options; and
- discussions with global peers (Royal Mail, New Zealand Post, Canada Post, Deutsche Post, Post Danmark, PostNL and Swiss Post) and postal industry experts (the International Post Corporation, Boston Consulting Group (BCG) and PricewaterhouseCoopers) to identify potential reform strategies and their impact.

The Departments of Communications and Finance also consulted around twenty Australian Government departments and agencies to identify key issues associated with the postal reform and possible impacts on their stakeholders. Consultants (BCG and Deloitte Access Economics), engaged by the Department of Communications to provide expert advice on Australia Post's letters business and broad options for reform, also consulted key departments as part of their analysis.

Key issues raised during the consultations included:

- postal organisations in developed countries are experiencing and responding to changing demand in postal services and falling letter volumes;
- there is need to address Australia Post's deteriorating financial position and minimise the risk of a future call on the Budget and taxpayer;
- Australia Post is an integral part of the Australian community and future reform needs to consider the impact on older Australians, small business and regional and remote communities;
- there is a need to ensure any future reform minimises post office closures in regional communities, reductions in postal service delivery and street post boxes;
- concerns by Australia Post's workforce and unions about the employment implications and impact on working conditions;
- reform will improve Australia Post's financial position, in turn allowing licensed post offices to remain viable into the future; and
- Australia Post must engage with unions, employees, small business and licensees about reforms and their implementation.

Further information on key issues raised is at **Attachment 4**.

Post-decision

Australia Post will continue to engage with key stakeholders during the reform implementation phase. A key element of its *Communications and Stakeholder Engagement Plan* involves continuing consultation with stakeholders to outline the reform agenda as well identifying specific issues and concerns about the reforms prior to their implementation. These stakeholders include Australia Post's workforce (employees, unions, licensee groups and mail contractors), major customers (small business, business and industry groups) and peak organisations representing regional and community groups, senior citizens and vulnerable and disadvantaged groups. This consultation is taking place between March and October 2015 and includes:

- continuation of the National Conversation Portal;
- roundtable meetings and workshops;
- face to face meetings, noticeboards, the Workforce Conversation Portal and telephone hotline (in the case of Australia Post employees);
- the establishment of a regional and rural consultative group and a monthly survey to track rural and regional sentiment; and
- a national teleconference with Australia Post licensees.

6. Selected option

On 3 March 2015, the Ministers for Communications and Finance issued a joint media release[30], announcing regulatory reforms would be made to enable Australia Post to modernise its business and ensure that it can continue to deliver an efficient and sustainable mail service. Australia Post also issued a media release[31] regarding the announced reforms, as well as a mail-out to all delivery points explaining the reforms.

Specifically, consistent with Option 3(c) considered above, the regulatory reforms will enable Australia Post to introduce a two-speed letter service – comprising Regular and Priority services.

The Regular service will be the CSO service for the purposes of the APC Act. Under this service, mail will be delivered a maximum of approximately two days slower than the current requirements. This service will be subject to pricing oversight by the ACCC and the Minister for Communications will retain the power to disapprove any price increase.

The Priority service will be a commercial service, with the Australia Post Board responsible for decisions on the pricing of the service. Australia Post will be required to continue to deliver the Priority service to the existing delivery timetable (e.g. daily, excluding weekends and public holidays, to 98% of delivery points).

[30] *Joint release with the Hon Mathias Cormann Minister for Finance: Reforming Australia*
[31] *Government supports Australia Post's plan to reform its letters service*

7. Implementation and evaluation

Key deliverables

Implementation of the agreed regulatory reform requires amendment to the:

- *Australian Postal Corporation (Performance Standards) Regulations 1998* (the Performance Standards); and
- *Price Notification Declaration (Australia Post Letter Services) (No.2) 2011* (the Price Notification Declaration).

Implementation of the Regular letters service will require amendments to the Performance Standards to vary the letter delivery speed standards. The revised regulation would be a disallowable instrument.

Application of the ACCC pricing notification arrangements to the Regular service will require the Minister for Small Business to:

- revoke the current Price Notification Declaration; and
- make a new Price Notification Declaration pursuant to section 95X of the *Competition and Consumer Act 2010* to apply the pricing oversight arrangements to the Regular service.

The new Price Notification Declaration would be a disallowable instrument requiring tabling in Parliament.

Australia Post has indicated that it will commence preliminary work on the necessary operational and service changes to implement the two-speed letter service (including workforce reforms and operational redesign). Once the amended regulation has been registered on the Federal Register of Legislative Instruments, Australia Post will notify the ACCC and the Minister for Communications of its intention to increase the price of the Regular service. The two-speed letter service will be introduced following the outcome of the ACCC's review and the Minister's consideration.

The ACCC has advised that, given the proposed changes in Australia Post's letter services and the ACCC's changed role in oversighting prices for Australia Post's letters service, it will need to develop new pricing oversight guidelines in consultation with Australia Post.

Australia Post will continue to report on the performance of all letter services as part of its existing reporting obligations, including on a quarterly basis.

Australian Government departments will need to consider the impacts of the changed mail delivery timeframes, especially for the Regular service, on their obligations with regard to communicating with their clients, and in particular any requirements that correspondence with clients must use the postal system. Any such provisions may require legislative and/or business process amendments.

Communications strategy

Following the announcement of the agreed regulatory reforms on 3 March 2015, the Australian Government and Australia Post initiated the agreed Communications Strategy. The objectives of the strategy are to:

- increase awareness and understanding of the challenges and the impacts of declining letter volumes on Australia Post; and

- outline the reform agenda including the proposed regulatory reforms, expected timing and likely impacts.

Timing of reforms

It is important that these reforms are implemented as quickly as possible. The amended instruments are disallowable in Parliament. Following the regulatory changes, the ACCC will complete a review of the proposed price increase, which could take from six to nine months. Implementation is therefore probable in early 2016.

Key milestones

The regulatory reforms are expected to be implemented as follows:

Milestone	**Expected timing**
Commencement of the regulatory amendment process – Department of Communications	March 2015
Implementation of the Communications Strategy – Australian Government and Australia Post	March 2015 – October 2016
Completion of regulatory amendment process (i.e. amended instruments tabled in and allowed by Parliament) – Department of Communications	2nd half of 2015
Introduction of a two-speed letter service and implementation of operational changes (following the passage of regulatory reforms through Parliament and a review of the proposed price increase by the ACCC) – Australia Post	early 2016

Review

Shareholder departments will monitor the impacts of the regulatory reforms and Australia Post's operational and letter service changes on the postal market and the broader community, including through consultation with Australia Post and other key stakeholders.

Shareholder Ministers will review progress and any further developments impacting on Australia Post's long-term viability.

Attachment 1

AUSTRALIA'S POSTAL REGULATORY FRAMEWORK

Australia Post

Australia Post is prescribed by the *Commonwealth Authorities and Companies Regulations 1997* as a Government Business Enterprise (GBE). Australia Post is established by the *Australian Postal Corporation Act 1989* (the APC Act) as a statutory corporation operating on a commercial basis at arm's length to Government, and the Board of Australia Post is accountable to two shareholder Ministers: the Minister for Communications and the Minister for Finance.

Australia Post's primary function is to provide postal services to everyone in Australia, no matter where they reside, at an affordable price. It does so to meet the social and commercial needs of the community. Australia Post also has international treaty obligations to do so as a member of the Universal Postal Union (UPU) of the United Nations.

Australia Post's community service obligations (CSO) are imposed on Australia Post through the APC Act. The APC Act requires Australia Post to supply a letter service that is 'reasonably accessible to all people in Australia on an equitable basis, wherever they reside or carry on business'[32]. In particular, the letter service must be available at a single uniform rate for standard letters carried by ordinary post ('the basic postage rate').

As a GBE, and under the APC Act, Australia Post also has commercial obligations to its principle shareholder, the Commonwealth (see below).

Australia Post's reserved services

Under the APC Act, Australia Post has the exclusive right to collect, carry and deliver letters within Australia that (subject to exceptions) weigh not more than 250 grams. This letters monopoly, along with the right to issue postage stamps, is Australia Post's 'reserved services'[33]. Australia Post was given this statutory monopoly so that revenue from its reserved services could fund the cost of meeting its CSOs[34].

Other letter services

Within the domestic reserved letter service, Australia Post offers a number of different categories of mail. Ordinary letter services are offered at three postage prices—currently $0.70 for small letters (the Basic Postage Rate – BPR), $1.40 for large letters up to 125 grams, and $2.10 for large letters over 125 grams and up to 250 grams.

The term 'other letter services' refers to those domestic reserved letter services that are not ordinary letter services. This includes categories of letters commonly referred to as 'bulk mail', given minimum volume requirements[35]. Australia Post also offers a range of other letter services, which

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[32] See Division 1 of Part 3 of the *Australian Postal Corporation Act 1989* (APC Act)

[33] Division 2 of Part 3 of the APC Act

[34] The 1989 explanatory memorandum for the APC Act stated: 'The right to carry letters within Australian and between Australia and overseas is reserved to Australia Post in recognition of the CSOs imposed on Australia.'

[35] Details of bulk mail categories

are used mainly by businesses, government agencies and not-for-profit organisations, and which are generally offered at prices lower than those of equivalent ordinary letter services.

These services are:

- PreSort Letters;
- Charity Mail;
- Acquisition Mail;
- Clean Mail;
- Impact Mail;
- Metered/Imprint Mail;
- Local Country Letters; and
- Reply Paid.

Further detail on these letter services is at **Annexure 1**. For the PreSort Letter and Charity Mail categories, mail senders have had the choice for over a decade of two delivery timetables. The 'Priority' timetable adheres to the Prescribed Performance Standards applicable to Australia Post's reserved letters service, while the 'Regular' timetable costs less but letters are delivered one to two days slower.

The choice of the two delivery timetables was extended to the Clean Mail, Imprint Mail and Metered Mail categories in June 2014. Two-speed delivery is now available for around 85% of total letter volumes. As of September 2014, around 70% of all eligible mail was being lodged via the Regular delivery service[36] (or around 60% of total letter volumes).

Coinciding with the increase in the BPR to $0.70 on 31 March 2014, Australia Post also introduced concession rate stamps, valued at $0.60. These are available to any Commonwealth Government concession card holder. To receive the concession, eligible customers are required to register for an Australia Post concession card, Australia Post has committed to maintain the price of the concession stamps at $0.60. Australia Post will also continue to offer all Australians the Christmas rate stamp at $0.65.

Australia Post's commercial obligations

A principal objective for Australia Post, as for other GBEs, is that it adds to shareholder value by, among other things, earning at least a commercial rate of return. This includes fully recovering the costs of resources employed, including capital, and working towards a financial target and a dividend policy agreed with Shareholder Ministers. The rate of return should be at least sufficient to justify the long-term retention of assets in the business, and to pay commercial dividends from those returns[37].

Similarly, the APC Act imposes commercial obligations on Australia Post. Section 26 of the APC Act imposes an obligation on Australia Post to, as far as practicable, perform its functions in a manner consistent with sound commercial practice. Section 38 specifies a number of matters that Australia Post must have regard to in setting financial targets, including the need to earn a reasonable rate of

[36] June 2014 Year End Report to Ministers, August 2014

[37] *Commonwealth Government Business Enterprise Governance and Oversight Guidelines*, Department of Finance and Deregulation, 2011, para. 1.8.

return on Australia Post's assets, the expectation of the Commonwealth that Australia Post will pay a reasonable dividend, and the need to maintain Australia Post's financial viability.

Additionally, under article 3.4 of the UPU convention, Australia is required to ensure that its universal postal service is provided on a viable basis, thus guaranteeing its sustainability[38].

For Australia Post to meet these commercial and international obligations, it is important that, to the maximum extent possible, its reserved letters service operates on a financially self-sustaining basis.

Regulatory framework

The Australian Government has sole responsibility for the regulation of Australia's postal industry. The government's aim is to provide a regulatory framework that contributes to Australia Post's ability to operate a viable and sustainable letters business, in the context of the CSO identified in the APC Act and the *Australian Postal Corporation (Performance Standards) Regulations 1998*.

Australia Post is also subject to the *Australian Postal Corporation Regulations 1996* and, as a Commonwealth Authority, is governed by the *Public Governance, Performance and Accountability Act 2013 (the PGPA Act)*.

Community Service Obligations

A community service obligation (CSO) arises when a service provider is required to undertake a non-commercial business activity to meet particular social objectives. Australia Post's CSO is imposed on Australia Post through the APC Act. The APC Act requires Australia Post to supply a letter service that is 'reasonably accessible to all people in Australia on an equitable basis, wherever they reside or carry on business'[39].

In particular, the letter service must be available at a single uniform rate for standard letters carried by ordinary post ('the basic postage rate'). Subordinate legislation sets the performance standards Australia Post must meet in providing its services (see discussion below).

The CSOs were included in the APC Act in recognition of the important role that written communications in the form of letters played in society at that time – noting that the APC Act came into effect prior to the wider availability of the Internet in the early 1990s. Given the societal importance of letters at that time, Australia Post is required to provide a letter service for both domestic and international traffic that:

- is reasonably accessible to everyone on an equitable basis
- operates to performance standards that ensure the service meets the social, industrial and commercial needs of the community and
- includes a standard letter service at a uniform rate Australia-wide.

There is a financial 'cost' associated with meeting the CSOs. The cost arises where the charges for mandated services do not recover the costs of providing them—the cost is measured on a net basis

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[38] Article 3.4 of the UPU convention

[39] See Division 1 of Part 3 of the *Australian Postal Corporation Act 1989* (APC Act)

after reduction of related revenue. Australia Post's CSO costs have increased over time, and were $203.5 million in 2013–14[40]. At the time the APC Act was enacted it was envisaged that profits from reserved services would be sufficient to fund CSO costs.

Since 2008–09, Australia Post's domestic reserved letter services as a whole have operated at a loss. Given that Australia Post must deliver its CSO regardless of whether the reserved services statutory monopoly delivers sufficient profits to fund the costs of the CSO, this cost has effectively had to be met from Australia Post's non-reserved mail business and other commercial activities[41].

Prescribed Performance Standards

Prior to 1998, Australia Post was responsible for setting and reporting on its performance in relation to the delivery of letters. Regulations made under Section 28C of the Act detail the particular performance standards (the Prescribed Performance Standards – PPS) to be achieved by Australia Post in meeting its CSOs. The PPS are outlined in the *Australian Postal Corporation (Performance Standards) Regulations 1998* (the Regulations), which prescribe minimum standards Australia Post must meet in delivering its letter service, including:

- delivery performance (94% of letters on time – as specified in the schedule at Item 6 of the Regulations and shown in the table below)
- minimum delivery requirements (98% of delivery points daily and 99.7% of delivery points twice a week)
- a minimum number and locations of retail outlets (4,000 outlets with 2,500 in rural or remote areas) and
- a minimum of 10,000 street posting boxes.

Australia Post's performance against the PPS is subject to independent audit by the Australian National Audit Office.

Address of letter	**Delivery time**
Letters for delivery intra-State:	
(a) within metropolitan area of capital city of lodgement	Next business day after day of posting
(b) within any other city or town of lodgement, or within adjacent town	Next business day after day of posting
(c) outside city or town of lodgement and adjacent towns	2 business days after day of posting
Letters for delivery inter-State:	
(a) within capital city metropolitan area if lodged in capital city metropolitan area of another State	2 business days after day of posting

[40] Australia Post Annual Report 2013-14. Australia Post calculates CSO costs on a long run avoided cost methodology. Therefore, these costs are not directly comparable with reserved services profitability figures, which Australia Post prepares on the basis of its full-cost absorption cost allocation model.

[41] The ACCC identified reserved letter services as a potential recipient of a cross-subsidy in 2009–10 on the basis that revenues were less than direct and attributable costs. See p. 13 of Assessing cross-subsidy in Australia Post *2009–10—An ACCC Report*

Address of letter	Delivery time
(b) within capital city metropolitan area if lodged outside capital city metropolitan area of another State	3 business days after day of posting
(c) outside capital city metropolitan area if lodged in capital city metropolitan area of another State	3 business days after day of posting
(d) outside capital city metropolitan area if lodged outside capital city metropolitan area of another State	4 business days after day of posting

Prices surveillance of the reserved services

Australia Post's reserved letter services are notified services (and Australia Post is a declared person) under the prices surveillance provisions of the *Competition and Consumer Act 2010* (the CCA)[42]. Australia Post must therefore notify the Australian Competition and Consumer Commission (the ACCC) if it proposes to:

- increase the price of a reserved letter service
- introduce a new service that would fall within the definition of reserved letter services
- provide an existing reserved letter service under terms and conditions that are not the same or substantially similar to the existing terms and conditions of that service.

In November 2011, the Treasurer issued the *Price Notification Declaration (Australia Post Letter Services) (No.2) 2011* under section 95X of the CCA, which reduced the scope of the prices surveillance that applies to Australia Post, leaving only ordinary letters (priced at the BPR) and large letters up to 250 grams subject to price regulation. This declaration is due to expire on 1 August 2016. Australia Post is able to charge freely for other services it provides, including offering bulk letter services at reduced rates based on the processing and transport costs avoided by Australia Post.

In accordance with the declaration, Australia Post must notify the ACCC of any proposed price increases in relation to its reserved services. The ACCC must then assess the proposed prices and decide whether or not to object to the increase. The ACCC's analysis will include an assessment of whether the proposed prices reflect an efficient cost base and offer a reasonable rate of return on capital.

Following the ACCC's decision, the Minister for Communications has the power, under s.33 of the APC Act, to disapprove the proposed increase within 30 days after receiving notice of a proposed determination from Australia Post.

The scrutiny by the ACCC is intended to promote efficient pricing and consumer protection where there is reduced competition.

[42] Prices surveillance provisions are found at Part VIIA of the CCA. The Treasurer has made a declaration pursuant to section 95X of the CCA

OTHER LETTER SERVICES

- The **PreSort Letters** service offers discounted prices to customers who can apply barcodes when addressing their letters, sort them into a particular order, place them in appropriately-labelled trays and complete documentation prior to lodgement at designated postal outlets. Australia Post offers the PreSort Letters service with regular and off-peak delivery time frames. The minimum lodgement volume is 300 barcoded letters of the same size and weight step.
- **Charity Mail** provides discounted prices for barcoded PreSort small letters sent by income tax-exempt charities. Mailings must meet all other requirements of the PreSort Letters service.
- The **Acquisition Mail** service allows customers to geographically target an addressed-mail campaign to residential addresses in specific postcodes, suburbs or Census Collection Districts. Letters must be barcoded, sorted into appropriately-labelled trays and lodged at designated postal outlets. The Acquisition Mail service is provided on the off-peak delivery time frame and has a minimum lodgement volume of 30,000 letters.
- **Clean Mail** is a service for smaller machine-addressed letters prepared in accordance with specific addressing and presentation requirements. Addressing conditions include certain mandatory requirements such as layout and font size and style. Articles do not require sorting but must be lodged in trays at designated postal outlets. Clean mail is provided at the regular delivery time frame and has a minimum lodgement volume of 300 letters.
- **Impact Mail** covers non-rectangular mail (such as shaped postcards, form-cut brochures, die-cut booklets or multidimensional folds) and attracts higher prices than ordinary postage prices. The minimum lodgement volume is 300 articles.
- Under the **Metered/Imprint Mail** service, a discount is available against ordinary postage rates where the postage is paid for by postage meter, or via the use of the ‘Postage Paid’ imprint (and payment by an Australia Post charge account).
- The **Local Country Letters** service provides for discounts where senders who reside or carry on a business in specified postcodes lodge letters at an Australia Post delivery office for delivery in that, or an adjoining, delivery area. The minimum lodgement volume is 50 letters (or 10 in small communities with fewer than 1000 delivery points).
- The **Reply Paid** letters service provides for the charging of mail recipients rather than senders. Some Reply Paid postage prices are higher than the equivalent ordinary postage prices as there are additional costs associated with extracting and counting the letters to bill recipients.

Attachment 2

OVERSEAS POSTAL EXPERIENCE

The decline in letter volumes being experienced by Australia Post is part of a broader international trend, and many overseas postal service providers have already experienced more significant declines in volumes than those confronted by Australia Post to date. The most significant falls have been experienced in Denmark, where volumes have declined more than 54% since their peak in 2001. Other countries that have experienced significant declines have been:

- United Kingdom – 40% since 2004
- New Zealand – 40% since 2002
- United States – 30% since 2006
- Canada – 24% since 2007.

As a result, overseas postal services providers are experiencing similar impacts on their financial sustainability and ability to provide services. Overseas providers have responded to these challenges in a range of ways including:

- Royal Mail (UK) – offers a two-speed letter service (First Class is D+1 [i.e. day of posting plus one day] at 62p and Second Class is D+2/3 at 53p). Mail is delivered 6 days/week to all households. Price caps have been removed from the majority of Royal Mail's products and services, though a "safe- guard" price cap will remain for second class standard and large letters, and standard packets up to 2 kilograms. There has also been separation of Royal Mail and the Post Office with Royal Mail being privatised.
- New Zealand Post – offers a two-speed letter service (FastPost is D+1 at $1.40 and Standard Post is D+3 at $0.80) and NZ Post must notify shareholders of proposed price increases. From July 2015, NZ Post must deliver at least 3 days/week to 99.88% of addresses.
- Canada Post – offers a single speed letter service at $0.85. Service is D+2 within a city, D+3 within a province and D+4 between provinces. Mail is delivered 5 days/week. Canada Post is moving away from delivery to the home, with the remaining one-third of delivery points transitioning to community mail boxes.
- Denmark – offers two-speed letter service (D+1 at €1.20 and D+4 at €0.87). Mail is delivered on all business days except Monday (though a Monday service is available to customers at extra cost).

STAKEHOLDER CONSULTATIONS – KEY ISSUES RAISED

Stakeholders	Consultation Process	Common themes
The Australian Government	Prior to the consideration of postal reforms by the Australian Government, the Departments of Communications and Finance consulted extensively with Australia Post and relevant Australian Government agencies to discuss the challenges faced by Australia Post and potential impacts arising from possible reforms. This included bi-lateral and inter-departmental committee meetings with twenty departments and agencies, especially extensive users of mail services and those with stakeholders likely to be impacted by the postal reform process.	• The need for a communications strategy to inform the public of Australia Post's circumstances and need for reform. • The impact of the reforms on small business, LPOs, regional employment and on international mail. • The impact of the slower speed service on vulnerable groups, regional and Indigenous communities. • The short term impact on departments who are required to use the Priority service in order to meet legislated delivery times. • The need to revise delivery times based on the current Ordinary mail service. • The increased use by government departments of online means of communication.
Australia Post – mail users (including regional communities)	<u>National Conversation Portal</u> A *National Conversation portal* seeking community views on, for example, the impact of the decline in letter volumes and the introduction of a two-speed letter service. More than 100,000 people visited the site since its launch in June 2014, with 35 % of visitors actively participating (i.e. through posting and voting).	• Participants were concerned about Australia Post running at a loss and agreed that action needs to be taken now to address the issues. • Participants from remote locations were concerned about how the reforms will affect them. • Participants noted that post offices are important to communities, particularly in regional and rural areas. • Participants agreed that Australia Post needs to 'take care' of the elderly, those who do not or cannot access technology and those living in regional and remote Australia. • Participants agreed on the need for long transition periods to enable people to adapt to change.
	<u>Community Discussion Groups</u>	• Participants expressed concern about Australia Post becoming a burden on the taxpayer and agreed that action needs to be taken.

STAKEHOLDER CONSULTATIONS – KEY ISSUES RAISED

	Australia Post conducted face-to-face community discussion groups, covering similar topics to the National Conversation portal.	• Participants from metro areas who would be least affected by change, were most open to potential changes, while those from remote areas were more resistant to change. • Participants from remote communities raised such issues as the reduction to service delivery, delays in letter delivery, loss of street post boxes and potential impacts of centralised distribution. • A reduction in the number of post offices was deemed least acceptable across all discussion groups.
	<u>Local Community Engagement Program</u> A local community engagement program, encompassing face-to-face local community discussion groups in various locations across Australia. This included hosting roundtable meetings with community leaders in 27 towns or regional centres across all states.	• Common themes included that Australia Post is vital to local communities, change is inevitable and Australia Post needs to be self-sustaining. • Participants were interested in the regular and priority letter service and wanted more information around costs especially for those on lower income and also for the elderly. • Concerns raised about rural communities and how Australia Post was going to manage the resources in these communities. • Participants noted that not everyone wants conduct business on a computer, and many still use the postal service.
	<u>Other Discussion Groups</u> During 2013 Australia Post conducted a range of discussion groups to survey reactions to different reform options.	• Participants were open to some limited reduction in current services being offered, for example, three times a week. • Participants were concerned about disadvantaging older, home-bound customers. • There was resistance to having letters delivered to post offices.
Australia Post - Small Business	Australia Post consulted with small businesses through focus groups to determine the level of acceptance of the need for change, and likely responses by different customer segments to a range of potential reform options. SMBs who used a variety of Australia Post services were recruited to	• Concerns around the impact on small businesses, especially around price increases. • General acceptance that the digital environment has reduced the need for large volumes of physical mail. • Only important communication is now sent by physical mail and that email is for transitory or interim documents.

	discuss their levels of acceptance with a number of reform concepts being considered. These concepts were introduced after levels of acceptance for the need for change were debated.	• A need to further educate SMBs on the problems affecting Australia Post.
Australia Post - Workforce	<u>Workforce Conversation Portal</u> The *Workforce Conversation Portal* is a secure dedicated conversation portal that includes information on the challenges Australia Post is facing. Employees including StarTrack employees could post comments on different conversation topics or ask a question.	• Concerns from workforce around job security and changes to their work environment – including shift changes; penalty rates; work/life balance. • Other common themes identified by Australia Post employees include impacts of the changes on the customer.
	<u>Briefing Sessions</u> *Briefing sessions by senior executives:* Australia Post's managing director, Group CEO and members of the Executive Committee visited all major capital cities and held briefing sessions with managers and supervisors and also visited employees. More than 30 mail facilities and post offices were visited with 2,000 people attending the events.	• In October 2014, the EGM of Postal Services and senior managers visited all major capital cities and some regional locations. The common themes identified from these sessions with managers and employees included: – Extended trading – Christmas period and Saturdays; – Digital mailbox; – MyPost; and – Reform. • Following the reform announcement in March, briefing sessions with employees were held across the Mail Network. The common themes raised by employees included: – Job security; – Priority and Regular services – pricing, volumes (business letters) and logistics of introducing potential operational changes; and – Working arrangements and entitlements.

STAKEHOLDER CONSULTATIONS – KEY ISSUES RAISED

	Roadshows *Postal services Roadshows* were held in 37 metro and regional locations, with over 1,800 Postal Services employees attending.	• The common themes identified from these roadshows included: – Extended trading – Christmas period and Saturdays; – Digital mailbox; – MyPost; and – Reform. – Job security; – Priority and Regular services – pricing, volumes (business letters) and logistics of introducing potential operational changes; and – Working arrangements and entitlements.
Unions	Unions are regularly consulted with by Australia Post as part of National, State and Local consultative forums in which the challenges of the organisation are discussed, including financial losses incurred as a result of declining mail volumes. In addition to Enterprise-level forums, specific Mail Network forums are held every two months.	• Unions recognise the need for reform to the letters business, however have concerns around employment and the impacts the reforms will have to community services, especially in regional and rural areas. • Unions are concerned around job losses and what the reforms will mean for Australia Post staff. • Unions are concerned around the pay for shift workers.
Licensee representatives	Senior Australia Post representatives have consulted with licensee representative groups individually, and as part of a formal licensee working group that has met regularly since it was established in 4Q 2014.	• Licensees recognise the need for reform to ensure Australia Post and licensed post offices (LPOs) remain viable into the future. Like Australia Post, licensees are impacted by changing demand for postal services, falling letter volumes and declining foot traffic. • Many licensees believe that any reform to improve Australia Post's financial position (e.g. stamp price increases) must flow through to LPOs via increased payments, to improve LPO network viability. • New business/revenue streams should be explored and made available to all licensees. • Licensees are keen to be consulted on and contribute to the implementation of any reforms to ensure their specific needs and perspectives are considered. There is some concern about the impact

		reform may have on workloads and sales. • As LPOs are at the 'frontline', timely and effective communication between Australia Post and licensees about any change is essential to help provide consistent messaging to the community.
Global peers and postal industry experts	International Consultations	• Postal organisations across the developed world are experiencing changing demand for postal services, falling letter volumes and declining post office foot traffic. • Common responses to these challenges are: – Price increases well above CPI; – Introduction of slower speed products; – Reduction in delivery days; – Introduction of a new labour model (using casuals or part-timers for delivery activities); – Reduction in the number of street posting boxes; and – Conversion of post offices into 'postal points'. • Without exception global peers and postal industry experts have stressed the importance of making the case for change to employees, business partners, customers and the community. • Australia Post also consulted with global peers and postal industry experts to identify potential reform strategies, with New Zealand Post, Canada Post, Post Danmark, PostNL, Deutsche Post, Swiss Post and Royal Mail as well as experts from Boston Consulting Group, the International Post Corporation and PricewaterhouseCoopers.