



Commission for
Communications Regulation

An Post's price application of 19 October 2012

Publication of correspondence

Information Notice

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An Coimisiún um Rialáil Cumarsáide
Commission for Communications Regulation

Abbey Court Irish Life Centre Lower Abbey Street Dublin 1 Ireland

Telephone +353 1 804 9600 Fax +353 1 804 9680 Email info@comreg.ie Web www.comreg.ie

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1 Letter from An Post dated 2 November 2012

Mr George Merrigan
Director – Market Framework
ComReg
Abbey Court
Irish Life Centre
Lower Abbey Street
Dublin 1

2 November 2012

Ref: An Post's Price Application

Dear George

I refer to your letters of 23 October 2012 and 26 October 2012.

On 3 February 2012, An Post submitted a Price Application for changes to charges for Universal Services weighing less than 50g in accordance with the Communications Regulation (Postal Services) Act No. 21 of 2011 ('the Act') and notified ComReg of amendments to other Universal Service Charges. An Post has since implemented the changes to charges for Universal Services weighing more than 50g¹.

An Post has provided to ComReg on 19 October 2012 a non confidential version of the Application in order to facilitate ComReg's consultation process. This version takes account of Decision Notice D08/12² and certain recommendations of Frontier Economics³ have also been addressed.

Your letters raise further issues which are dealt with below.

Information Requirements to support Price Application:

In your letter of 23 October you state that *"The first task of ComReg staff will be to ensure that An Post's application contains all of the information necessary to conduct a full review of the application....."*

¹ On 1 May 2012

² ComReg document 12/81, Postal Regulatory Framework, Implementation of the Communications Regulation (Postal Services) Act 2011

³ ComReg document 12/109a, Frontier Economics Review and assessment of An Post's application for changes to the charges for postal services within the scope of the universal postal service. P. 41

Since submitting the Price Application in February, ComReg appointed Frontier Economics to review the Application and Analysys Mason to review An Post's compliance with the Accounting Direction. An Post has co-operated fully and provided all the information requested by ComReg and both sets of consultants to facilitate their respective reviews. In Appendices 1 and 2, I have set out the details of the significant volume of information provided to ComReg, Frontier Economics and Analysys Mason.

An Post would also point to the following statement made in your letter of 7 June which states "*ComReg will try to complete its review of An Post's application This has been facilitated by An Post having now provided much of the data required by ComReg.....*". Also in the minutes prepared by ComReg in relation to the meeting on 23 May, ComReg stated "*ComReg noted it appears that sufficient information is now in place to review the application*".

An Post, therefore, considers that it has to date fully co-operated and provided ComReg with all the relevant information to facilitate its review of the Price Application and is not aware of any further information that could be provided to ComReg or that ComReg could possibly require in order to commence a public consultation on the Price Application.

An Post's Compliance with the Accounting Direction:

You also state in your letter of 23 October that "*this review will also be linked to and affected by the separate project relating to An Post complying in full with all provisions of the 2006 Accounting Direction*".

An Post has prepared and submitted to ComReg Regulatory Accounts for the year end 31st December 2011. These Accounts were audited by KPMG. In fact for the first time, the audit report was addressed to both An Post and ComReg. ComReg had welcomed this development in its Information Notice⁴,

"The Commission currently requires. ... An Post... to procure certain assurances from a qualified independent body in respect of certain audited financial information on an annual basis. These assurances are generally in the form of audit opinions provided by audit firms... To date, the opinions provided by the auditors... have only been provided to and for the benefit of those companies, and have not included a duty of care to the Commission.

Following discussions during the past two years.... it has been agreed that these future audit opinions will include an express duty of care to the Commission...

This is a significant development in Ireland. It is intended that it will ensure a more efficient and transparent process.."

⁴ ComReg Document 12/19 - Accounting Separation:
ComReg agrees new 'duty of care' arrangements with regulated entities and their auditors

An Post also fully co-operated with ComReg's appointed consultants to review An Post's compliance with the Accounting Direction.

It appears, based on your letter, that the review of the Price Application may be *'linked to and affected by'* the review of the Regulatory Accounts. In light of the fact that there is a KPMG audit report in respect of these accounts and the auditors' duty of care is now to both ComReg and the Company, there is no basis for such a link and this is an unnecessary frustration at this late stage.

The following points all refer to your letter of 26 October:

Universal Postal Services set by SI 280 of 2012:

SI 280 of 2012 defines "Postal Packets Deposited in Bulk" as *'a substantial number of similar postal packets deposited with a universal postal service provider at the same place and time, to be transported and distributed to the addressees as marked on each of the postal packets'*. Section 3.1 (j) of the regulation requires An Post to provide a service for the *'clearance, transport and distribution of "postal packets deposited in bulk" for "deferred delivery"'*.

ComReg refers to paragraph 5.85⁵ of its response to consultation which states that the Regulation will be drafted to include the specific provisions of Discount A and Discount B. The Regulation is not drafted to reflect the terms of these bulk mail services. Paragraph 5.85 also states that the service to be specified is a composite of seven existing services. Paragraph 5.86 goes on to state that ComReg expects the two services (Discount A and B) as being likely to encompass the majority of postal packets posted at special bulk mail tariffs.

An Post comments on this are as follows:

- The actual Regulation does not specify the exact specifics of the deferred bulk mail service. Paragraph 5.89 says that the *'exact specifics of the bulk mail services as "universal postal services" (e.g. minimum volume requirements etc will be approved by ComReg in its approval of the bulk mail terms and conditions..'* Based on this statement, An Post is working on the basis that it is up to it to set out its proposals and for ComReg to approve these or not.
- ComReg also stated that the service is a composite of seven existing deferred services.
- Discount A and B do not represent a majority of postal packets posted at special bulk mail tariffs. In fact, they represent only a tiny fraction of this mail. ComReg has stated that the bulk mail universal services will represent the majority of postal packets posted at special bulk tariffs.
- Ceadunas facilities are only available to customers posting 2,000 items or more in a single mailing.
- The majority of mail posted at special bulk tariffs is, in fact, posted under Discount 6 which requires a minimum 85%+ auto-sort rate. If this is eliminated, the operation of the postal network will become less efficient as customers will not be obliged to keep databases etc up to date in order to avail of this discount.

⁵ ComReg document 12/81

An Post had interpreted SI 280 as it was presented, without any specifics included in relation to the deferred bulk mail service. The guidance set out in paragraph 5.85 sets out some detail but also says that it is a composite service and the exact specifics of the service will be approved with the bulk mail terms and conditions.



Also, it is worthwhile noting that as An Post proposes to maintain almost all current bulk mail services (with the exception of discounts 2 and 8), and as they are either services specified by ComReg as Universal Services or are services which are within the scope of the Universal Service,⁶ ComReg must give its prior consent to any change to tariffs for these services for items weighing up to 50g. Therefore, it is, to some extent, academic for the purposes of the Price Application which services are the designated Universal Services and which are not as ComReg must approve all price changes for items weighing less than 50g.

In relation to the new "Insured Service", this is not a Universal Service weighing less than 50g for which An Post is seeking to change a tariff and, therefore, does not form part of the Price Application. This is being dealt with in a separate process and An Post will forward details to ComReg in due course.

For information, the insured fee will be in the region of €5 plus the appropriate postage. This is based on an absolute requirement that a signature is obtained on delivery as otherwise this service would be open to fraudulent claims.

Non-discrimination:

- An Post is not proposing a payment method discount for packets and parcels. The reasons for this are:
 - The majority of items sent are paid by stamp or label. In fact, there are very few bulk packets within the USO. There are no bulk parcels.
 - The cost savings for metered and bulk letters derive mainly from machineability of these items which is not relevant to packets and parcels, which are processed completely by hand.

⁶ As per An Post's Notification and Declaration of 31 August 2012 (ComReg form 12/81n)

- An Post has provided its justification to ComReg for the proposed payment method discount of 5c for meter and bulk letters. This was set out in our response to Question 2 of the pack provided on 4 May 2012.
- An Post has set out in its response to Question 11 provided on 4 May 2012, its justification for the 5% discount proposed for buying stamps on-line. This is an initiative aimed at the SME market. We would have anticipated a warm welcome for this initiative from ComReg.
- The existing Registered service operates at a substantial loss. Even eliminating the cost of insurance claims will still mean a loss will be incurred. In fact, An Post should be seeking an increase higher than the one being sought in order to be truly cost oriented. (See Appendix 3 for details.)

Cost Orientation:

This section sets out ComReg requirements in relation to costing information for each price point. Notwithstanding the above section, which explains that sufficient information has been provided to ComReg to allow it to process the application, this section sets out the history of this particular requirement⁷.

Following the issue of the Accounting Direction⁸, An Post was required to provide to ComReg a timed Programme for Compliance with the Direction. On 5 February 2007, An Post provided this plan to ComReg. In relation to the particular section (Section 3.2), An Post stated

'At present, cost information at the level of each individual weight step is not available. A significant project will need to be undertaken to establish this information.'

On 10 March 2008, ComReg issued to An Post a Review of An Post's Accounting Data, prepared by LECG. This document made no reference to the requirement to produce accounting information by every individual price point.

On 24 October 2008, ComReg issued a letter to An Post stating the following

'ComReg will shortly issue a proposed draft template, setting out how, in its view, the Regulatory Accounts need to be presented in order to fully comply with the accounting Direction (including supplementary schedules and additional information).' (emphasis added)

These templates did not require An Post to provide the costing information at each price point. A subsequent letter of 12 December 2008 also did not mention this aspect as an item to be included in the work programme for the future.

In fact, this issue has not come up at all for five years since the issue of the accounting Direction until this Price Application was submitted.

An Post would also make the following points:

⁷ Section 3.2 of the 2006 Accounting Direction, ComReg document 06/63

⁸ ComReg document 06/63

- The Price Application is for Universal Service items weighing less than 50g. There is only one weight break involved for each of the services and the cost has been provided to ComReg.
- An Post has, in any event, made an estimate of costs per unit per price point for the vast majority of mail volumes. In fact, most items are letters which only have one weight step. The details that were provided by An Post cover the vast majority of items.
- There are no guidelines provided by ComReg as to how an estimate is to be made. It is clearly not as detailed as the Regulatory Accounts or the term 'estimate' would not be used. An Post has made an estimate based on its judgment
- ComReg also asks '*Why are some proposed price points higher than their estimated costs?*' The implication is that ComReg is of the view that all services must be provided either at or below the cost of providing the service.

Affordability:

An Post does not agree with the statement made by ComReg in relation to affordability. An Post has provided elasticity estimates, average spends for SMEs, referred to various research undertaken including that commissioned by ComReg⁹ in this area which didn't have price as the most important factor for these businesses when considering postal services.

An Post has also explained to ComReg that any further research asking customers if they were willing to pay higher postage costs is a fruitless exercise.

ComReg is also planning to consult publicly on the proposals; all interested parties will have an opportunity to voice their concerns. An Post has had no significant adverse reaction to its price changes for items weighing more than 50g, implemented in May this year. An Post has also had no feedback whatsoever to the publication by ComReg of the details of the Price Application in the Frontier Report¹⁰. The report sets out for the first time publicly the key details of the An Post Price Application.

Terms and Conditions:

The process to approve the Universal Service terms and conditions is a separate process to the Price Application. An Post does not understand why these have to be dealt with together. In fact, they are treated separately in ComReg's work programme set out in its recent Postal Strategy Statement¹¹.

We had agreed in previous correspondence¹² that the most efficient manner to progress the approval of Terms and Conditions was by meeting and An Post remains available to meet to progress this issue.

⁹ ComReg document 10/102a – Report by Research Perspective

¹⁰ ComReg document 12/109a issued on 9 October 2012

¹¹ ComReg document 12/116. See timeframe reference 3, Approve or amend terms and conditions for universal postal service, P.52.

¹² See correspondence of 4 January, 18 June, 19 June and 25 June 2012.

However, in order to facilitate the process, An Post is attaching its response to the comments provided by ComReg in its working document dated 6 September 2012. An Post will provide a marked up amended version of the terms and conditions following ComReg's comments on this response.

Financial data - Group Net Cash:

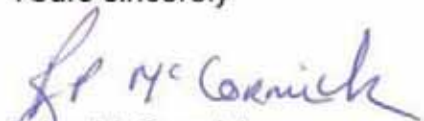
The Group Net Cash figure has nothing to do with the Universal Service. This figure is not required in order for ComReg to make a decision on the Price Application.

Conclusion:

The ongoing significant loss in the provision of the Universal Service is a burden that is materially affecting the financial sustainability of An Post. The current Price Application is both justified and urgently required. We originally engaged with ComReg on the Application in December 2011 and made our formal Application in February 2012. Given the current financial position of the USO, and by extension An Post, we would request that the Application is given the urgent attention that it deserves.

I would be grateful if you could confirm that you have been provided with all the relevant information to review our Price Application and confirm that the public consultation will proceed in line with the indicative timetable which you set out at our meeting of 2 October 2012, i.e. that a public consultation could take place six weeks following the submission of the non confidential version of the Price Application and updated forecasts.

Yours sincerely

A handwritten signature in blue ink that reads "B. McCormick". The signature is written in a cursive style with a large initial 'B'.

Brian McCormick
Services Director

Appendix 1- Information provided to ComReg and Frontier Economics as part of their review of An Post's Price Application

Information Submitted to ComReg	Date Submitted to ComReg
Application for changes to charges for Universal Services weighing less than 50g in accordance with the Communications Regulation (Postal Services) Act No. 21 of 2011 ('the Act') and Notification of amendments to other Universal Service Charges.	3 rd February 2012
Completed Excel template in format prescribed by ComReg. (ComReg also required forecasts categorised by pay and non pay despite the Accounting Direction requiring a categorisation by product pipeline).	4 th April 2012
Report prepared by Indecon Consultants on Price Elasticities used in the Price Application.	4 th April 2012
Market Research supporting the Price Application.	4 th April 2012
International Benchmarking supporting the Price Application.	4 th April 2012
Response provided to 60 Questions raised by ComReg on the Price Application.	4 th & 15 th May 2012
Response to Information request by Frontier Economics.	6 th June 2012
Response to a further Information request by Frontier Economics.	20 th June 2012
Response to a further Information request by Frontier Economics.	25 th June 2012
Response to a further Information request by Frontier Economics.	5 th July 2012
Response to Frontier Economics draft Report.	13 th September 2012
Non Confidential Version of the Price Application including updated forecasts.	19 th October 2012

Appendix 2- Information provided to ComReg and Analysys Mason as part of their review of the Accounting Direction.

Information Submitted to ComReg	Date Submitted to ComReg
Initial "kick off" meetings with ComReg and Analysys Mason including a visit to the DMC to observed the RMS	22 nd March 2012
Response to initial information request by Analysys Mason. (This request included inter alia the RMS Results and various outputs from SAS ABM.)	2 nd April 2012
Response to a further Information request by Analysys Mason.	13 th April 2012
Response to a further Information request by Analysys Mason.	17 th April 2012
Meeting with ComReg and Analysys Mason, including a visit to DMC & AMC to observe the RMS.	22 nd /24 th April 2012
Response to a further Information request by Analysys Mason	25 th April 2012
Response to a further Information request by Analysys Mason	26 th April 2012
Response to a further information request by Analysys Mason.	3 rd May 2012
Response to a further Information request by Analysys Mason	11 th May 2012
Response to a further Information request by Analysys Mason,	16 th May 2012
Response to a further Information request by Analysys Mason	18 th May 2012
An Post submitted its review and assessment of Analysys Mason's draft report.	23 rd July 2012
Response to "Final" Information request by Analysys Mason.	8 th August 2012
Further Response to "Final" Information request by Analysys Mason.	21 st August 2012
An Post intends to respond to the Final report by Analysys Mason which was submitted to ComReg on the 15 th October 2012	Due to be sent on 15 th November 2012

2 Letter from An Post dated 6 November 2012

Mr. Alex Chisholm
Chairperson
ComReg
Abbey Court
Irish Life Centre
Lower Abbey Street
Dublin 1.

6 November 2012

Ref: An Post's Price Application

Dear Alex

I refer to the issue of the sustainability of the Universal Service and wish to bring to your attention the grave concerns I have in respect of this issue, particularly in regard to An Post as the universal postal service provider. As you are aware, ComReg's objectives as set out in the Communications Regulations (Postal Services) Act, 2011 include the primary objective *'to promote the development of the postal sector and, in particular, the availability of a universal postal service within, to and from the State at an affordable price for the benefit of all postal service users'*¹. The Regulatory Accounts for 2011 were audited by KPMG and the audit report was addressed to both An Post and ComReg thereby including an express 'duty of care' to ComReg as requested. These accounts highlight that An Post incurred losses of €50m in the provision of Universal Services in 2011. This is forecast to increase to in excess of €60m in 2012 (even allowing for changes arising from ComReg's decisions in relation to the Postal Regulatory Framework²). To date, these losses have been funded by An Post from its other activities. While An Post will continue to endeavour to finance losses in the provision of the Universal Service, as far as is practicable, losses of this magnitude are simply not sustainable and An Post cannot finance them in full from its other activities into the future.

An Post has held its headline tariff at 55c since March 2007. However, it became clear to An Post in the summer of 2011, in light of the decline in mails volumes, that significant increases in prices for Universal Postal Services would be required in addition to the significant cost reduction programme already in place. The primary driver behind this is a structural decline in traditional mail volumes which has the impact of increasing the "per unit cost" of the mail service. This conclusion was reached having considered the full extent of costs savings already achieved and achievable in the coming years across the entire An Post organisation.

¹ Section 10

² ComReg document 12/81

In the period since 2007 there has been a decline in the traditional mail volume of c. 30%. The company has succeeded in reducing its annualised costs by €100m per annum (which is more than 15% of the cost base). As the postal industry has witnessed worldwide, cost reduction alone cannot deal with the structural issues impacting the industry and significant price alignment is required.

Other national postal operators have come to the same conclusions in relation to the challenges being faced worldwide by the industry and, as a result, price increases can be seen across the industry worldwide. In the UK prices were increased in April 2011 and again in April 2012 (the latter increase being 30%). The current headline tariff in the UK for First Class mail is 60p (75c).

As the benchmark data for the industry demonstrates, mail prices in Ireland are amongst the lowest in Europe and have now fallen almost 30% behind the UK price model which still remains one of the lowest in Europe. Royal Mail's price is the one that applies in Northern Ireland.

Having identified the requirement, we included appropriate pricing policies and price adjustments in our rolling five year business plan from mid 2012, we advised our Board who approved these adjustments in December 2011 and we also presented the business plan including the price increases to our shareholding Department of Communications, Energy and Natural Resources. The Department of Expenditure and Public Reform were also briefed of our intentions in regard to price increases. These briefings took place in December 2011 and I also offered you the same facility in early 2012 which you did not wish to take up.

The formal submission of the current Price Application was made in February 2012.

The manner in which this application has been dealt with by your organisation is causing real difficulties for An Post as we are still not aware when, if at all, we will be able to increase the headline tariff. There has been a relentless list of queries, information requests and expensive reports commissioned from consultants from outside the State. Whilst we have dealt with all of your organisation's queries, we believe that many have been unnecessary, too detailed in nature and have caused unnecessary delay. Additional hurdles have also been raised at a late stage. It is not clear to us that ComReg fully understands the real financial difficulties which An Post is attempting to address. The conclusions from the ComReg commissioned Frontier Report simply highlight that there is uncertainty ahead. That does not mean that we take no action. Mail volumes which are likely to be lost to electronic alternatives are in all probability going to be lost whether the increase is approved or not. The reality is that these reviews actually substantiate and re-enforce the case for immediate price increases and a policy which will allow for further adjustments over the coming years.

There is an unnecessary financial difficulty being created for An Post arising from the current regulatory price controls and process. As the primary role of the regulator is to ensure the ongoing sustainability of the Universal Service, I believe it is incumbent on us to highlight this to you and your organisation and to urge that you take steps immediately to rectify the situation before it gets completely out of hand and the Company is forced into an entirely unnecessary financial crisis as a result of the regulator's inaction. A possible consequence of this may be the undermining of the provision of the Universal Service, which ComReg is statutorily obliged to protect.

I have had to inform the company shareholding Department of the situation and the consequences of not achieving a timely resolution to this issue. We firmly believe An Post requires early approval of its current Price Application and that there needs to be a fundamental change in the regulatory approach to requests for price increases going forward. A financially stable Universal Service should be the core long term objective for all key stakeholders, including An Post, its customers and employees, ComReg and the Government and we have demonstrated that we are committed to playing our part in achieving this. The postal industry worldwide has price alignment as a key part of the strategy and this is likewise required for Ireland.

The Price Application was submitted over nine months ago. All the information available to An Post has been provided to ComReg in support of the Price Application. We have no doubt that more than sufficient information is now available for ComReg to make an informed decision on the Price Application. I now call upon you to ensure that the current Price Application is put to public consultation without further delay and that your postal team engages with us constructively in formulating realistic pricing policies for the future which will ensure the sustainability of the Universal Service.

I look forward to a positive response so that we can plan towards a financially sustainable Universal Service for the benefit of all.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Donal Connell', written in a cursive style.

Donal Connell
Chief Executive

**3 Letter from ComReg to An Post dated
15 November 2012 in reply to An
Post's letter of 6 November 2012**



15 November 2012

Mr Donal Connell
Chief Executive
An Post
GPO
O'Connell Street
Dublin 1

Ref: An Post's amended price application

Dear Donal,

I refer to your letter of 6 November 2012 concerning An Post's application to increase its tariffs for certain postal services within the scope of the universal postal service relating to postal packets weighing less than 50 grams, and to the relationship which you draw between that application and the funding and future sustainability of the universal postal service.

You state that the tariffs at issue, which include An Post's "headline tariff" of 55c, are not sufficient to cover the costs which An Post claims to be incurring in providing the universal postal service. You state in that regard that An Post's audited Regulatory Accounts show an incurred loss of €50m for 2011 resulting from the provision of the universal service, a figure which you expect to increase to €60m for 2012. You also state that it became clear to An Post in the summer of 2011 that significant price increases would be required to address those losses in addition to the significant cost reduction programme already in place. For that reason, An Post now seeks to increase certain tariffs, to include a 10c (or 18.18%) increase in its "headline tariff", which requires the prior consent in writing of ComReg in accordance with section 30(12) of the Communications Regulation (Postal Services) Act 2011 ("2011 Act").

Please note that as your letter has been submitted to ComReg in the context of an application made under section 30(12) of the 2011 Act, which will involve public consultation before ComReg makes its final determination, a non-confidential version of your letter will be published by ComReg in due course together with this response letter and all other relevant correspondence. This shall be done in accordance with ComReg's published Consultation procedures (Doc 11/34) and its Guidelines on the treatment of confidential information (Doc 05/24).



Commissioner Kevin O'Brien and I are most concerned about the financial situation which you describe, given ComReg's mandate to ensure the availability of a universal service and An Post's role as the current sole provider of the universal service, and we wish to ensure that there is full and proper engagement between ComReg and An Post on this important matter, and that we be kept informed of the latest financial projections within An Post insofar as they relate to the provision of the universal postal service. In this regard, we are particularly concerned to note that the situation appears to have deteriorated since An Post shared its Five-Year Plan with ComReg and is now descending into what you describe as a potential "financial crisis". In this regard, ComReg would welcome any update on An Post's Five-Year Plan, particularly as regards revised mail volume or cost containment estimates.

In setting out my response, I first step through certain provisions of the 2011 Act which I think are relevant to An Post's application and the stated basis for that application, as I think it worthwhile to distinguish between these provisions by explaining their particular purposes. Next, I address the comments in your letter as to the manner in which you consider ComReg has dealt with An Post's application. This is followed by some comments on the potential effects of a price increase, which I make by reference to the recent Frontier Economics Report, commissioned and published by ComReg (Doc 12/109a). I conclude with some remarks about the wider challenges facing the postal sector in Ireland, in which An Post has such a central role.

Statutory Framework

ComReg is at all times aware of its primary statutory objectives as set out in section 12 of the Communications Regulation Acts, 2002 – 2011. You refer to and quote the first of those three objectives which is "*to promote the development of the postal sector and, in particular, the availability of a universal postal service within, to and from the State at an affordable price for the benefit of all postal service users*". I also refer you to the closely-connected statutory function, set out in section 10 of the Act, which is "*to ensure the provision of a universal postal service that meets the reasonable needs of postal service users*".

However, in addition to ComReg's overarching statutory function and objectives, other provisions of the 2011 Act are also relevant to the issue at hand. In particular, I would point to the fact that an application to increase tariffs, made under section 30(12), is different to an application for funding of the universal postal service, made under Chapter 5 (sections 35 & 36). These are separate and distinct statutory provisions, designed for different purposes, and each has its own process and set of determinative criteria. I describe each of these provisions under the headings below. Please note that I do so in an effort to present an overview and I do not purport to set out the provisions in detail or definitively, nor do I offer any indication as to how these



provisions might be applied by ComReg in the current circumstances or possible future circumstances.

Universal Service funding – Chapter 5 of the 2011 Act

An application for funding of the universal postal service, made under Chapter 5, begins with An Post submitting a request in writing to ComReg which is made in the "form and manner" as determined by ComReg. ComReg shall then determine whether the universal service is a "net cost" and whether as a result it represents an "unfair financial burden" for An Post. If ComReg makes those two determinations then section 36(1) provides that "*it shall apportion the net cost among providers of postal services within the scope of the universal postal service and such providers shall make a contribution, in accordance with the cost apportioned to each of them, for the purposes of meeting that burden*". In making such determinations, ComReg must also take into account (a) the methodology used by An Post with respect to the information provided by it, and (b) the extent to which An Post is complying with its statutory obligations to provide the universal service *in a cost-efficient manner*.¹ Chapter 5 thus requires ComReg to assess the net cost of providing the universal service, if any, by reference to a cost-efficient provider of that service.

I have referred to Chapter 5 of the 2011 Act, though I accept that An Post has not sought to invoke its provisions nor indicated its intent to do so. Nevertheless, by An Post's own figures (which have yet to be confirmed and accepted by ComReg) it is clear that the losses which An Post claims it is incurring would not be covered by the tariff increases which An Post seeks to introduce. There would still be a significant shortfall between revenues and losses, even if those increased tariffs were introduced as per the application, and their financial impact was as predicted by An Post.² Subject to An Post explaining how the remaining deficit would be made up, I can only take these approximate figures to indicate a likelihood of An Post making an application under Chapter 5 in the near future. If that is a possibility, then I consider that I am obliged to point out that even if ComReg was to determine that the universal service did constitute an unfair financial burden for An Post, the only action available to ComReg would be to apportion that net cost among "*providers of postal services within the scope of the universal postal service.*"

This category of contributors would include An Post itself, in its capacity as a provider – indeed the predominant provider - of services which are not

¹ Section 35(5) of the 2011 Act. Italics added.

² The Frontier Report refers to An Post's estimate that the requested tariff increases which require ComReg's prior consent would increase its annual revenues by c. €16m in its first full year of implementation, while An Post projects an incurred loss of c. €60m for providing the universal postal services in 2012. Using An Post's own figures, this would leave a remaining deficit of c. €44m. The same report expresses concern that An Post's estimate of the financial benefit of the price rise sought may be 'optimistic'.



"universal postal services" but are "postal services within the scope of the universal postal service"³ This is a very important point because logically it must mean that any current or imminent financial problems with regard to funding of the universal service will largely or entirely need to be resolved by An Post itself. The structure of the 2011 Act, coupled with An Post's very substantive share of the Irish postal market, means that An Post would be by far the largest contributor to any universal service fund. While ComReg has not formally calculated the potential contributions of other postal service providers, it is likely that any contributions from other postal service providers operating within the scope of the universal service are likely to be quite small relative to the size of the deficit which An Post says exists. Therefore, for all practical purposes, and so far as we are aware, there is little or no source of funding of the universal postal service beyond An Post itself.

Price increase application – Section 30(12) of the 2011 Act

Section 30(12) is essentially an interim provision, covering the period of time between the final increase to charges in the former "reserved area"⁴ and a replacement five-year price cap decision made under section 30(1) of the 2011 Act.⁵ ComReg is required to consider an application under section 30(12) by reference to the five "tariff requirements" set out in section 28(1), which include requirements that tariffs shall be affordable, cost-oriented and non-discriminatory. An Post must demonstrate compliance with these tariff requirements and this requires substantial analysis and supporting information. In this respect, ComReg commissioned Frontier Economics to assist it in its review. Frontier Economics reported on their review and, following consideration of this report, An Post agreed to submit an amended price application.

The requirement that any tariffs which are adjusted under section 30(12) shall remain "affordable" and "cost-oriented" can be read in conjunction with (a) ComReg's overarching objective "*to promote ... the availability of a universal postal service ... at an affordable price ...*", and (b) the requirement under section 35(5)(a)(ii) that an assessment as to whether the universal service represents an unfair financial burden shall include an assessment of the extent to which the service is being provided in a cost-efficient manner. These various provisions thus reflect one another, though they are separate and distinct.

You will appreciate, in this regard, that ComReg is bound by statute to consider any application made under section 30(12) by reference to the tariff requirements. This means in effect that ComReg can only consent to a price increase where it is satisfied that the increased prices would still be affordable

³ ComReg "Guidelines concerning 'postal services within the scope of the universal postal service'", published on 26 July 2012 (Doc 12/81a).

⁴ Section 70 of the 1983 Act, as inserted by Regulation 8(4) of the Postal Regulations 2002.

⁵ The Postal Strategy Statement states that ComReg plans to implement a price cap by the end of 2013, following public consultation.



for postal service users and would reflect the relevant incurred costs of An Post.

Comments re: ComReg's handling of the price increase application

Though I am required to reply to your comments regarding the manner in which you consider that ComReg has dealt with An Post's application, in doing so I must first state that I would prefer our organisations to have a co-operative and productive relationship, insofar as possible and appropriate. It is the role and responsibility of you and your Board to ensure An Post's financial viability, while it is ComReg's responsibility, as you rightly point out, to promote the availability of the universal service for the benefit of all users. Although these responsibilities are not the same, they are connected and they require that we should work together. Hence once I have responded for the organisation, as I must, to the various points you have raised in relation to ComReg's conduct, I would propose that we put such disagreements aside, and move forward on the substantive issue of the financial and other challenges which you say are affecting An Post.

You state that ComReg's handling of the price increase application is causing real difficulties for An Post and that "*a relentless list of queries, information requests and expensive reports*" have been too detailed, and have caused unnecessary delay, and that it is not clear that ComReg appreciates the financial difficulties in which An Post finds itself. You also assert that all information available to An Post has been provided to ComReg in support of its application to increase its charges and that you have no doubt that more than sufficient information is now available to ComReg to make an informed decision.

In reply, I must first observe that you state that it became clear to An Post in the summer of 2011 that there was a problem with funding of the universal service, and yet an application for a price increase under section 30(12) of the 2011 Act was not received by ComReg until 3 February 2012, some six to eight months later. Further, ComReg staff provided An Post officials with a schedule setting out the required information on 27 January 2012, in advance of the application being made. However, on assessing the application submitted by An Post on 3 February, ComReg staff found it to be lacking certain information, which they then requested by letter dated 16 March 2012. I refer to this and other relevant correspondence and key dates set out in the Appendix to this letter, which show that ComReg has acted as expeditiously as possible throughout this process, whereas An Post has failed to provide all of the required information despite the requirement having been made clear from the outset, thereby delaying its own application which it says is most urgent.

Therefore, such delay as has occurred cannot simply be attributed to ComReg. I must also refute your claim that sufficient information is now available to ComReg to make an informed decision, since not all of the



information has been provided, despite the requests for same. I must also refute your assertion that ComReg has made relentless information requests, some of which have been unnecessary or too detailed in nature, and that this has caused delay. Without going into detail of matters which have been the subject of correspondence and discussions at an operational level, the information requested is simply that which ComReg requires in order to determine if a price increase of more than 18% on the standard domestic letter is justified and necessary. Further, the information requests have not been "relentless", though some have been made more than once, for the simple reason that information requested was not provided.

As I stated above, I am required to reply to your comments. However, I again confirm that we do wish to move forward, and ComReg is prepared to proceed to public consultation as soon as possible, once all of the remaining information has been provided to it by An Post. The ComReg postal team is at all times willing to engage fully with your officials and I note, in this regard, that George Merrigan is writing separately to Brian McCormick in order to progress this same issue.

Potential effects of a price increase

Your summary of the conclusions of the Frontier Economics Report, commissioned by ComReg, causes us some concern, as you state that those conclusions "*simply highlight that there is uncertainty ahead*". I would encourage An Post to reflect carefully upon the Frontier Economics Report and its implications before finalising its amended price application, as the report sets out quite specific concerns with regard to An Post being over-optimistic on two critical matters: (1) the rate of further decline in letter volumes; and (2), the impact of the proposed price increases on customer behaviour (and hence net financial impact).

In your letter, you urge ComReg to take steps "*to rectify the situation before it gets completely out of hand and the Company is forced into an entirely unnecessary financial crisis as a result of the regulator's inaction*". While I must first refer to my earlier comments and deny that there has in fact been any inaction or delay on ComReg's part, I also confirm that ComReg is committed to preventing any such crisis to the fullest extent possible and consistent with its statutory remit.

However, in doing so not only must ComReg ensure that any future prices are affordable and based upon a cost-efficient operation but must also take into account such relevant factors as consumer behaviour, including price elasticity. As you will appreciate, a significant price increase is only ever a solution to excess costs or falling volumes if enough customers are willing to accept and absorb the increase.

I note, in this regard, that you state that An Post's incurred losses in providing the universal service are the result of a c.30% decline in traditional mail



volumes since 2007, which you attribute to structural issues which are impacting the postal industry worldwide. I presume that the key structural issue which you refer to is "e-substitution", the ongoing trend of traditional postal services users switching to alternative electronic communication services, such as email and e-billing, which is essentially a global occurrence and is not caused by regulation or liberalisation of postal markets. I also presume that the decline in mail volumes is to some extent a result of the general economic downturn since 2008.⁶

In light of such a decline in mail volumes in just five years, and the fact that many customers and particularly larger business customers are replacing their traditional postal service with electronic substitutes, it is clearly necessary to assess carefully the impact of a proposed price increase of nearly [REDACTED]. Would enough customers accept and absorb the increase so as to make it worthwhile, or would so many customers switch to an electronic substitute or other delivery method as to reduce substantially, or even remove completely, the net gain to the provider? Price increases, if excessive, could accelerate the downward trend in letter volumes, thereby jeopardising, rather than ensuring, the sustainability of the universal service.

I do not mean to suggest or imply that ComReg has formed a view that price increases in the amount sought would have such an adverse effect, but merely that the question is a relevant one and must be properly considered, especially in an economic climate where An Post's business customers, who account for most of its mail volumes, and which includes the State⁷ itself in its various forms, are considering every cost they face. Hence we do not necessarily subscribe to your stated view that "*Mail volumes which are likely to be lost to electronic alternatives are in all probability going to be lost whether the increase is approved or not*". This will be a point for the forthcoming public consultation.

⁶ Chapter 16 of the *Report of the Review Group on State Assets and Liabilities*, published in April 2011, states that in common with most postal services internationally, An Post faces a difficult trading environment in the coming years, and identifies the following foreseen challenges:

- *A significant drop in postal volumes because of the economic downturn with an allied drop in turnover. Some of this business will not come back to An Post (declining postal volumes is a worldwide phenomenon).*
- *The continuing threat to both the postal and post office business from electronic substitution.*
- *Full opening of the postal market to competition from 2011 leading to a possible threat from competitors for large volume business.*
- *The industrial relations challenge of aligning the company's fixed cost base to declining revenues particularly in the postal business.*

⁷ Larger customers adopting electronic communications technologies includes the State itself – see, for example, the 2007 Special Report on "eGovernment" published by Office of the Comptroller and Auditor General



What is essentially at issue here is the same overarching objective which you refer to, namely ComReg's duty to ensure "*the availability of a universal postal service ... for the benefit of all postal service users*" which must include assessing the potential effects of any proposed price increase upon the financial sustainability, and hence the availability, of that service. ComReg considers that price alignments are appropriate once they do not have such adverse effects as described above, and are in all other respects in line with the requirements of the 2011 Act. In this regard, I note that a price increase to match inflation could be appropriate, especially noting the passage of time since An Post last increased prices in letters up to 50g (2007), and that CPI changes are specifically referred to as an element in the new price cap regime that must be put in place.

Conclusion

In this letter, I have tried to explain how ComReg is conducting its work and the relevant statutory requirements, including the criteria by which ComReg will make any future determination under section 30(12) of the 2011 Act. I have also responded to certain inaccurate statements contained in your letter regarding ComReg.

I have also endeavoured to show how in reality the future financial sustainability of An Post, and hence of the universal service, is very largely in the hands of An Post itself, and must therefore be the responsibility of you, your Board, your workforce, and your shareholders. Accordingly ComReg encourages you to take all necessary actions to address any financial problems which are identified.

One action of immediate use and relevance would be to direct your staff to provide all outstanding information in respect of the price increase application. Once this is done, ComReg will proceed as soon as possible with its public consultation and thereafter will form its determination, in accordance with the statutory provisions outlined above and based upon all relevant information before it, including responses to the consultation. I refer to ComReg's recently published Strategy Statement which states that ComReg plans to initiate the consultation this year with a decision to issue in Quarter 1 of 2013, though once again this is subject to all required information having been provided by An Post.

Much of the information provided by An Post will also be used by ComReg in future projects, including implementing a 5-year price cap next year, which will require realistic forecasting, strong supporting data which conforms with the Accounting Direction, and timely and constructive engagement from An Post.

I must, however, re-iterate that the figures provided by An Post indicate that even if ComReg were to give its consent to the price increases which are



sought, and even if those increases were accepted by enough An Post customers so as to make the increases worthwhile, then this would still not address the financial problem which you say is occurring and which is presented as being the reason for the price increase. According to An Post's own figures (which have yet to be confirmed and accepted by ComReg) there would still be a substantial annual cost deficit arising from the provision of universal postal service.

Further, as the relevant provisions of the 2011 Act coupled with the current structure of the Irish postal market indicate that the universal service will mostly be funded by An Post, one way or another, I must encourage An Post to do everything possible to address its finances and to balance its operations budget so as to match its revenues, rather than rely on some form of regulatory relief. In this regard, appropriate price adjustments may well be necessary, but they must be considered very carefully in light of the profound changes taking place in the wider communications sector, which includes both postal *and* electronic communications services. Any such increases must form part of a much wider programme of adjustment to address falling mail volumes, to include continuous efforts to reduce revenue loss by improving efficiencies and the quality, value and choice on offer to customers, and measures to develop new revenue streams (including outside the core mails business) and to manage costs in lines with revenues.

As noted at the outset, your letter will be published in due course as part of ComReg's public consultation and so I would ask that you please advise of any commercially sensitive material therein which you wish to have redacted, in accordance with ComReg's published Guidelines on the treatment of confidential information (Doc 05/24).

Finally, I wish to reiterate on behalf of ComReg our commitment both to a constructive engagement with yourself and your company, and to the fulfillment of all of our statutory functions and duties.

Yours sincerely

Alex Chisholm
Chairperson



Appendix:

Application dated February 2012

27 January 2012	ComReg send to An Post schedule setting out the information required to review a price application. This schedule is based on one previously sent to An Post on 29 April 2004.
3 February 2012	An Post submit application. An Post application includes Downstream Access as universal postal service even though working definition (05/85) did not include it as such. An Post make major assumption that most of its bulk mail customers will switch to this Downstream Access service if it is a universal postal service.
16 March 2012	ComReg completes initial review and notes application is not complete and did not conform fully to the schedule sent to An Post on 27 January 2012. ComReg request An Post to provide the missing required information
30 March 2012	An Post informs ComReg that An Post is increasing prices for >50g with effect from 1 May 2012. These price increases do not require ComReg's prior consent.
4 April 2012	An Post revert with information requested by ComReg on 16 March 2012
18 April 2012	ComReg notes that information supplied 4 April is still incomplete. Nonetheless, detailed review questions sent by ComReg to An Post.
30 April 2012	ComReg publishes draft decision setting 'de minimis' universal postal services. Downstream Access is not and cannot be universal postal service but will consider responses to the supporting consultation.
4 May 2012	An Post revert with answers to most of ComReg's detailed review questions of 18 April 2012.
11 May 2012	ComReg notes to An Post its draft decision relating to 'de minimis



Communications Regulation

	universal postal services and that Downstream Access is not and cannot be universal postal service.
28 June 2012	Frontier present initial findings to An Post following their review of price application.
26 July 2012	ComReg decision issued specifying 'de minimis' universal postal service. Consistent with 05/85. Downstream Access is not a universal postal service.
30 August 2012	An Post informed that the Frontier Report is being finalised following consideration of An Post views following the presentation of 28 June, following decision in relation to 'de minimis' universal postal service, and following consideration of work to date on parallel workstream in relation to compliance with Accounting Direction.
6 September 2012	ComReg send draft Frontier Report to An Post for comment on (1) any errors or factual inaccuracies (2) confidential redactions
13 September 2012	An Post revert with comments and redactions sought. An Post state will make amended application following consideration of Frontier report.
27 September 2012	ComReg reply to An Post that their comments have been considered by Frontier and all redactions sought have been accepted
9 October 2012	In the interests of transparency, ComReg publish redacted version of Frontier report and supporting Information Notice

**4 Letter from ComReg to An Post dated
15 November 2012 in reply to An
Post's letter of 2 November 2012**



Commission for
Communications Regulation
Coimisiún Um
Rialáil Cumarsáide

15/11/2012

Mr Brian McCormick
Director Services
An Post
GPO
O'Connell Street
Dublin 1

Ref: An Post's price application of 19 October 2012

Dear Brian

I refer to your letter dated 2 November 2012 and I address below the points raised in that letter. Please note that as your letter has been submitted to ComReg in the context of an application which will require public consultation, a non-confidential version of your letter will be published by ComReg in due course, together with this response and all other relevant correspondence. This shall be done in accordance with ComReg's published Consultation procedures (Doc 11/34) and published Guidelines on the treatment of confidential information (Doc 05/24).

Information requirements to support a price application

As you are aware, An Post's pricing of its universal postal services must comply with the tariff requirements of the Communications Regulation (Postal Services) Act 2011 ("2011 Act"). These include the requirements of affordability, non-discrimination, and cost orientation. By necessity, demonstrating compliance with these requirements will require detailed supporting information and analysis and ComReg can only review an application once it has been provided with all the necessary information.

In your letter, you question what further information ComReg could require to review An Post's amended price application. I am surprised by this question given an amended price application is being made by An Post to include, for the first time, the full specification of the universal postal services set by ComReg on 26 July 2012 in the Communications Regulation (Universal Postal Service) Regulations 2012 (SI 280 of 2012). As you acknowledged in your letter of 13 September 2012, as a result of this specification in July, an amended price application is required from An Post as there are a number of universal postal services that are different from those set out in An Post's original price application of February 2012. Therefore, the pricing of these revised universal postal services, for example the new Proof of Delivery facility, require additional detailed supporting information.

Commission for Communications Regulation
An Coimisiún um Rialáil Cumarsáide

Block DEF, Abbey Court, Irish Life Centre, Lower Abbey St, Dublin 1
Bloc DEF, Cúirt na Mainistreach, Ionad Irish Life, Sráid Na Mainistreach Iocht, Baile Atha Cliath 1
Telephone +353 1 804 9600 Fax +353 1 804 9665 Email info@comreg.ie Web www.comreg.ie



Against this background, ComReg staff have conducted an initial review of An Post's amended application of 19 October 2012 and have now also conducted a further review of the amended price application and the detail you supplied with your letter of 9 November. This review was conducted by ComReg staff in order to assess whether all the required information to support the pricing of the specification of the universal postal services set in SI 280 of 2012 on 26 July 2012 is now available to ComReg. Following these reviews, ComReg staff remain of the view that all the required information has still not been provided by An Post. Therefore, in order to fully review An Post's price application, please find in the appendix to this letter a listing of the required information.

An Post's compliance with its Accounting Direction

Given the requirement for An Post's prices for its universal postal services to be cost-oriented, I am surprised by your statement that there is no link between the review of An Post's compliance with the Accounting Direction and the price application and that such a link "*an unnecessary frustration at this late stage*". The Accounting Direction sets an obligation on An Post to provide a cost estimate for each price point and ComReg will examine these cost estimates, and how they were calculated, in its assessment as to whether An Post's proposed prices are cost oriented.

Universal postal services specified

In respect of the bulk mail services specified as universal postal services, ComReg specified these clearly in the Communications Regulation (Universal Postal Service) Regulations, 2012 (SI 280 of 2012) and supporting D08/12. It is for An Post to ensure that its universal postal services comply with the Regulations. Therefore, the "Deferred Delivery" bulk mail universal postal service must be specified in accordance with SI 280 of 2012 and D08/12.

In relation to the Insured Service which is specified as a universal postal service, ComReg requires supporting information from An Post that demonstrates its proposed pricing for its Insured Service is compliant with the tariff requirements of the 2011 Act. This information should have been sent when An Post made its price application. Therefore, ComReg sought information on the pricing and costing of this universal postal service in its letter of 26 October. However, An Post in its reply of 2 November did not provide this required information and said this information will be provided to ComReg "*in due course*". ComReg requires this information to review An Post's price application. Consequently, this required information has been requested again in the appendix to this letter.

Non-discrimination

As stated in previous correspondence and Information Notice 12/109, ComReg will ensure that there is no pricing discrimination by An Post against any group of postal users. In particular, ComReg will ensure that any discounts are supported by the cost avoided for that discount alone. Therefore, ComReg again seeks the information on the costs avoided for those discounts alone in the appendix to this letter.



Cost orientation

We note that the Accounting Direction obligation on An Post to make an estimate of the cost for each price point is clear and in effect since the implementation of the Accounting Direction. I further note that to be compliant with the tariff requirement of cost orientation for each price point does mean that prices should be at or below the cost estimated for that price point. Therefore, in the appendix to this letter, ComReg seeks further information as to how these cost estimates were made.

Affordability

We would disagree that a survey of business and SME postal users in relation to the affordability of the price increases is a "*fruitless exercise*". To ensure the provision of the universal postal service and to understand any likely impact on volumes, I would consider such a survey would be very useful. Furthermore, such a survey was conducted by An Post for its residential postal users so clearly there is some merit in such surveys.

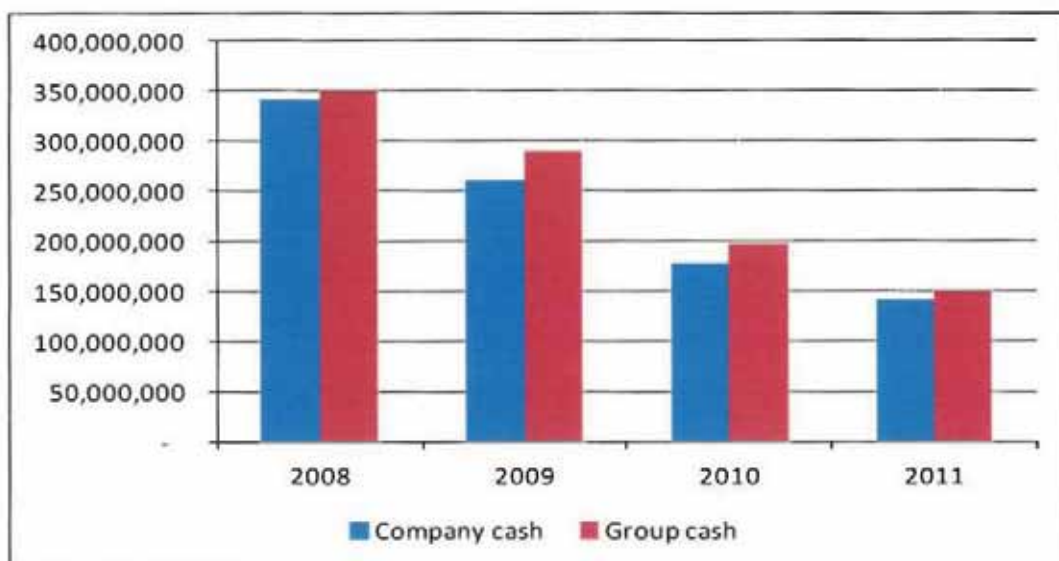
Terms and conditions

We disagree that the terms and conditions for universal postal services is a separate task. They are linked as the terms and conditions set out the exact details of the universal postal services including the schedule of charges. This linkage is acknowledged by you earlier in your letter of 2 November. Therefore, in the appendix to this letter, ComReg again seeks the proposed terms and conditions for the universal postal services.

Financial data – Group net cash

We strongly disagree that An Post's projections for its group net cash have nothing to do with the ensuring the provision of the universal service. ComReg has been tasked with ensuring the provision of the universal postal service and therefore can validly seek information as to the overall financial position of the postal service provider which has been currently designated a the universal postal service provider.

In this respect, ComReg is concerned by the deteriorating cash position of An Post which is reproduced overleaf based on information from An Post's audited and published financial statements:



As can be seen above, based on An Post's published and audited annual reports, An Post is losing c.€50-€90m cash a year. Given the cash balance of €150m at the end of 2011, and absent any other changes (e.g. cost reductions commensurate with the volume reductions), this means An Post could run out of money in two years. We recognise that An Post's 5 year plan which was made at the end of 2011 has made assumptions to address this and to maintain a cash balance of c.€100m; however, we require an update on this given that 2012 is almost complete, for example, where the 5 year plan forecast cost savings for 2012 achieved?

We further note that, according to An Post, the proposed price increases will result in a c.€17m additional revenue in the first full year (subject to volume projections being correct). Therefore, as noted by An Post's own five year plan, significant cost reductions and additional revenue are required in order to maintain An Post's financial viability and in turn ensure the provision of the universal postal service.

Conclusion

To conclude, contrary to your statement, we note that formal engagement on An Post's price application commenced with your initial application of February 2012.

As set out in this and previous correspondence, once ComReg has all the required information to review the amended application, I can confirm that the amended price application will be consulted on by ComReg. Subject to all the required information being made available from An Post, ComReg plans to conduct this public consultation before the end of the year. Consequently, I request that all the information sought in this letter is provided by An Post by 29 November 2012 at the latest.



Finally, and as noted at the outset of this letter, your letter will be published in due course as part of ComReg's public consultation and so I would ask that you please advise of any commercially sensitive material therein which you wish to have redacted, in accordance with ComReg's published Guidelines on the treatment of confidential information (Doc 05/24).

Yours sincerely

**George Merrigan,
Director, Market Framework**



Appendix:

Required information to be provided by An Post by 29 November 2012

This information is required from An Post because the information cannot be obtained from any source other than An Post and the information is required in order to enable ComReg carry out its statutory functions and objectives set by the 2011 Act.

- 1) An Post to confirm in writing that it has provided all information it has in its possession, including all updates to information previously provided to ComReg, that relate to the price application.
- 2) An Post to provide full justification for the updated 2013 and 2014 growth rates. In particular, please provide an explanation of the differences between these figures and those used in the initial price application. Please also include an explanation as to why these growth rates do not differ between stamp, meter and bulk, despite the differences between these in 2012. This explanation should cover both domestic and international outbound mail.
- 3) An Post to provide full details (including pricing) for the insurance universal postal service. An Post to confirm that the cost of insurance is [REDACTED]
- 4) An Post to provide all materials, research, sales manager documentation in its possession that relate the affordability of the proposed price increases for its business customers.
- 5) An Post to provide full supporting explanation and rationale as to how it made its cost estimate for each price point charge it proposes to change and why these estimates are appropriate for ensuring that prices are cost oriented. For example, the explanation will address why "[REDACTED] of collection, transport and delivery costs varying with weight (excluding common costs)" was considered to be appropriate by An Post and not another % or another methodology.
- 6) An Post to provide all materials in its possession that relate to the proposed discounts for meter customers and buying stamps online. These materials would include costing and profitability analysis.
- 7) An Post to provide all materials in its possession that relate to the specification of the "Deferred Delivery" universal postal service.
- 8) An Post has notified a bulk mail product that An Post considers to be within the scope of the universal postal service and which An Post has called "Downstream Access". ComReg does not agree that this bulk mail service should be called "Downstream Access" as it leads to unnecessary confusion with the negotiated access under s.33 of the



2011 Act. An Post is to provide full details on the proposed pricing and take-up for this new bulk mail product.

- 9) An Post to all materials, papers / presentations, financial analysis in its possession that relate to addressing the losses on International Inbound which are c [REDACTED] n per annum.
- 10) An Post to provide full explanations for the differences in cost per unit between the per unit cost of "proof of delivery facility" (using historic registered service cost data) and the per unit cost of standard letter and the per unit cost of standard parcel. These full explanations will demonstrate that the proposed pricing for the new "proof of delivery facility" is cost oriented. In this respect, for example, the explanation should address why registered has a per unit common cost allocation of [REDACTED] compared to a per unit common cost allocation of [REDACTED] to standard letter.
- 11) An Post to provide any material in its possession that relate to the introduction of a meter payment discount for flats and packets.
- 12) An Post to provide full explanation for the fall in forecast cost savings by the end of 2012 from [REDACTED] to [REDACTED].
- 13) An Post to confirm in writing that the proposed tariff for Metered Letters and Bulk and Business Reply Letters is 0.60, as stated in the updated Pricing Application and 'App 2 Revenue and Volumes Model 2010-2014', and not 0.65, as stated in 'App 1 Proposed Prices'.
- 14) An Post to provide any material in its possession that relate to past and future e-substitution by its top 20 customers.
- 15) Following the price increases of 1 May 2012, all material in An Post's possession relating to the impact on volumes and profitability as a result of those price increases.
- 16) An Post to provide the proposed terms and conditions (including the schedule of charges) for the universal postal services specified in the Communications Regulation (Universal Service) Regulations 2012 (SI 280 of 2012). This was requested by ComReg in correspondence dated 6 September 2012 and most recently in correspondence dated 26 October 2012.
- 17) To assist ComReg's review of cost orientation, An Post is to provide the cost per unit detail as set out in the table on the next page with full supporting explanations for material (>5%) annual changes in cost per unit by individual category (e.g. Pay: collection).



	2008				2009				2010 – An Post to confirm below is correct				2011		
	Stamped letter	Meter letter	Ceadunas Letter	Stamped letter	Meter letter	Ceadunas Letter	Stamped letter	Meter letter	Ceadunas Letter	Stamped letter	Meter letter	Ceadunas Letter	Stamped letter	Meter letter	Ceadunas Letter
Pay:															
-Collection															
-Delivery															
-Inward sort															
-Other															
-Outward Sort															
-Revenue collection															
-Transport															
Non Pay:															
-Collection															
-Delivery															
-Inward sort															
-Other															
-Outward Sort															
-Revenue collection															
-Transport															
TOTAL PER UNIT COST															



- 18) An Post to provide cost estimates for:
- a) Business reply letters
 - b) Business reply large envelopes
 - c) Business reply packets
 - d) International outbound parcel: Zone 2, Zone 3, Zone 4
 - e) Sending books abroad: Zone 2, Zone 3, Zone 4
 - f) International outbound proof of delivery: Zone 2, Zone 3, Zone 4 for letter / packet / parcel respectively
 - g) IBMS: by letter/flat/packet by country where increased charge sought.
- 19) In relation to the amended forecast, An Post to provide full explanation to support the amended forecast and to provide all materials in its possession justifying that amended forecast made. These materials should also include a sensitivity analysis of different forecast(s) outcomes if they were made.
- 20) In relation to the amended forecast, An Post to explain the forecast volume losses on 'Deferred before noon' letters which are forecast to happen regardless of the proposed price increase.
- 21) In relation to the amended forecast, An Post to explain the forecast volume losses on 'Early presentation' letters which are forecast to happen regardless of the proposed price increase.

**5 Letter from An Post dated 29
November 2012 in reply to ComReg's
letter of 15 November 2012 (letter no.
4)**

Mr. George Merrigan
Director, Market Framework
Commission for Communications Regulation
Abbey Court
Irish Life Centre
Lower Abbey Street
Dublin 1

29 November 2012

Re: Price Application

Dear George

I refer to your letter of 15 November 2012. We are responding to you with the information that you have requested. Throughout the process we have responded with urgency to all requests for information either from ComReg itself or its appointed consultants.

An Post has also provided a significant volume of information to Frontier Economics in their review of An Post's Price Application and to Analysys Mason in their review of An Post's compliance with the Accounting Direction.

This information includes:

- A comprehensive overview of the Regulatory Accounting systems, which included a full list of all costs for the mails business (as per the general ledger) and how each of these costs flows through to the Mails business unit and then to individual products and services including full details on all cost drivers and allocation methods.
- Revenue and Volume calculations for all services.
- Sampling Results from the Real Mail Study (RMS) for 2009, 2010 and 2011 used in the calculation of revenues and volumes.

Recent Developments

It is worthwhile reviewing the most recent developments in this area.

In November 2012, Copenhagen Economics¹ delivered a presentation on its findings on *"Pricing behaviour of postal operators and its effect on postal markets"*, commissioned by the European Commission. The recommendations include the following:

- Allow more price flexibility to operators, in particular, relaxing the cost orientation requirements
- Assess the need for price caps and adjust accordingly. The principle being recognised here is that a conflict arises between declining volumes, which increase the costs per unit and the affordability principle which may mean that prices cannot increase, leading to a loss making situation. However, affordability may not be an issue at all. The specific recommendation is to ensure that price caps take account of declining volumes.

Further details will emerge on these recommendations in December but they are important in the context of the An Post Price Application. In particular, the recommendation to reflect the fact that volume decline increases costs per unit and that price caps should reflect this reality. An Post wishes to emphasise again that ComReg must take the impact of declining volumes into account in its consideration of the proposed price changes.

In addition, it is worthwhile recalling that Royal Mail has recently been given more pricing flexibility with certain regulatory safeguards included. The reason Ofcom, the UK regulator, provided this flexibility was:

*"In this uncertain time, where the position of post in relation to electronic substitutes is unclear, Royal Mail is in a better position to determine the impact of price rises of different products on overall demand and, hence, revenues."*²

I wish to comment on some of the general issues which you raised in your letter.

Information Requirements to Support a Price Application

ComReg must approve any change in tariffs for items weighing less than 50g, not only for the services set out in the Communications Regulation (Universal Postal Service) Regulation 2012 (SI 280 of 2012)('the Regulations'), but also any services falling within the scope of the Universal Service. Therefore, in effect, ComReg are continuing to review the same services as before the making of these Regulations.

In the appendix to your letter, a number of items of information are being requested for the first time in this Price Application process. This is disappointing as time is being lost in securing a much needed price increase for An Post. Examples of this include:

- Question 9 in the Appendix seeks details in relation to addressing losses in inbound international mail.

¹ Presentation to European Commission on 20 November 2012. We understand that the final report is due on 17 December 2012.

² Ofcom – Securing the Universal Postal Service: Proposals for the future framework for economic regulation, October 2011

- Question 17 which requires an analysis of costs for 2008-2011 by pipeline split by pay and non pay. No information in relation to 2008 or 2009 was sought before as part of the Price Application process. The split of total costs by pay and non pay was sought from 2010 onwards but not split by pipeline.

An Post's Compliance with the Accounting Direction

The audit of the Regulatory Accounts contains an express 'duty of care' to both An Post and ComReg. An Post has also co-operated fully with ComReg's appointed consultants in reviewing the compliance with the Accounting Direction. An Post has provided ComReg with a timed implementation plan dealing with the recommendations from this review.

Universal Postal Services Specified

An Post agrees that the "Deferred Delivery" bulk mail service must be specified in accordance with the Regulations. The Regulations require:

"A service for the clearance, transport and distribution of "postal packets deposited in bulk" for "deferred delivery"" (Section 3(1)(j) of the Regulations)

An Post's proposals meet with this definition and we believe will be welcomed by our customers.

An Post fully accepts that it must implement ComReg's direction in relation to Insured Services but again emphasises that this is not a postal packet weighing less than 50g for which we are looking to change a tariff. This is a service which the Regulations require An Post to implement. We are in the process of doing this.

Cost Orientation

An Post disagrees with ComReg on its interpretation of what 'cost-oriented' means. ComReg states that it *'does mean that prices should be at or below the cost estimated for that price point'*. There is no legal or economic basis for this argument. Section 28 (1)(b) of the Communications Regulation (Postal Services) Act 2011 ('the Act') requires:

"prices shall be cost-oriented, that is to say, that prices shall take account of and reflect the costs of, providing the postal service or part of the postal service concerned"

It does not say that prices should be at or below the costs estimated for each price point. ComReg's view would mean that An Post is obliged to provide the Universal Service at a loss no matter what it does. This is incorrect. An Post is entitled, subject to the affordability principle, to at least recover its costs. The term 'cost oriented' is not defined and there is no further guidance other than what is stated above and therefore it is not clear how ComReg can make this statement.

As mentioned earlier, declining volumes mean that costs per unit increase in spite of significant overall costs savings. This creates a difficulty in assessing what costs are

avoided as these will change from year to year depending on the rate of volume decline for each service. Therefore, reasonable ranges of costs avoided are more appropriate. This is in line with the recommendation of Copenhagen Economics to relax the cost orientation principle.

It is also worthwhile recalling the Frontier Economics conclusion in relation to An Post's price proposals:

'A comparison of unit costs and An Post price proposals suggests that the changes An Post is proposing would improve cost reflectivity'.³

Terms and Conditions for Universal Services

Terms and conditions need to be approved by ComReg regardless of whether An Post is pursuing a Price Application. There should be a separate process to allow for these to be approved independent of the Price Application process.

In order to progress this matter, a 'tracked changes' version of the Schedule of Charges is provided to ComReg on a confidential basis. The Terms and Conditions will be forwarded as soon as possible.

Financial Data - Group Net Cash

Group Net Cash is not a matter to which ComReg should have regard when considering this Price Application. The cash position cannot be analysed in the simplistic manner set out in your letter.

Your analysis is for a period commencing just after An Post had received a sizeable amount from the sale of assets. This was a deliberate strategy to raise funds to invest as follows:

- A 'catch up' on capital investment which was necessary. In the four years from 2004-2007, An Post invested an average of €12m p.a. in the business. This is insufficient for this business. In the five years 2008-2012, An Post has invested €35m p.a. on average in the business. This reflected the catch-up phase due to under investment prior to 2007.
- An Post has also invested in voluntary severance schemes which have allowed it to generate costs savings of €100m p.a.

These were deliberate actions and do not represent the underlying cash flow run rate in the business. Therefore, the analysis presented in your letter is flawed.

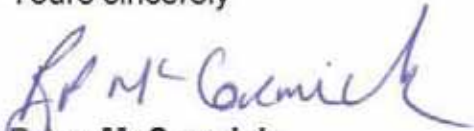
An Post has set out its plan in terms of continued cost reductions, price increases and new revenues from non Universal Services. An Post is committed to funding the losses in the provision of Universal Services from its own resources, as far as practicable, but requires price increases to keep this commitment to a reasonable level.

³ ComReg document, 12/109a, Review and assessment of An Post's application for changes to the charges for postal services within the scope of the universal postal service, Frontier Economics, P. 13

Conclusion

An Post believes that it has provided more than sufficient information throughout the process and co-operated fully with both reviews undertaken by ComReg. We welcome your commitment to undertake a public consultation on the Price Application before the end of the year.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Brian McCormick', with a stylized flourish at the end.

Brian McCormick
Services Director

In Commercial Confidence
APPENDIX:

Required information to be provided by An Post by 29 November 2012. This information is required from An Post because the information cannot be obtained from any source other than An Post and the information is required in order to enable ComReg carry out its statutory functions and objectives set by the 2011 Act.

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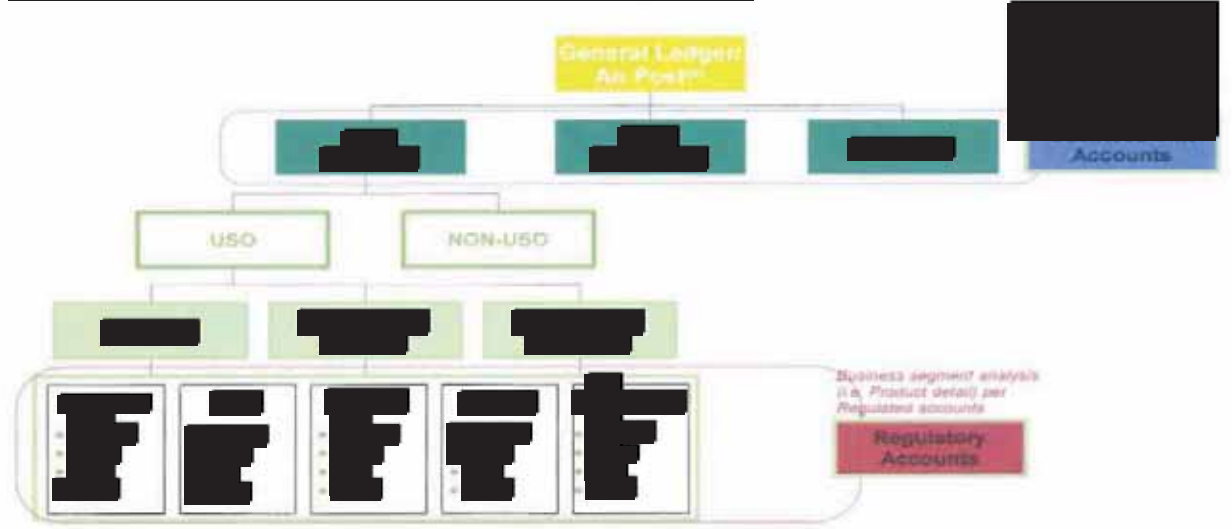
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6 Letter from ComReg dated 4 December 2012 in reply to An Post's letter of 29 November 2012



04/12/2012

Mr Brian McCormick
Director Services
An Post
GPO
O'Connell Street
Dublin 1

Ref: An Post's price application of 19 October 2012

Dear Brian

I refer to your letter dated 29 November 2012.

Please note that as your letter has been submitted to ComReg in the context of an application which will require public consultation, a non-confidential version¹ of your letter will be published by ComReg in due course, together with this response. This shall be done in accordance with ComReg's published Consultation procedures (Doc 11/34) and published Guidelines on the treatment of confidential information (Doc 05/24).

Recent developments

In response, to your review of recent developments in relation the pricing of postal services I can only state that ComReg must act within its statutory remit as set by the Communications Regulation (Postal Services) Act 2011 ("2011 Act"), while all matters of policy are reserved to the Oireachtas.

Information requirements to support a price application

I agree that time is being lost in An Post securing such a price increase as may be appropriate. However, as set out in our correspondence to date, this is because An Post had not provided in full all of the relevant information which ComReg required, and had repeatedly requested. The information provided recently remains lacking in certain cases, however, notwithstanding this, and in order to obtain the views of all interested parties, ComReg will proceed with the consultation on the price application with the aim, subject to An Post's prompt assistance where required, to publish its consultation by 21 December 2012.

¹ It is noted that An Post for its letter of 29 November has claimed confidentiality only in respect to the Appendix and supporting Schedules of the letter. By separate correspondence, ComReg has requested, in the interests of transparency, that An Post submit a non-confidential version of the Appedix and supporting Schedules by 10 December as this information will form part of the reasoning for ComReg's preliminary view on the consultation



An Post's compliance with its Accounting Direction

ComReg is reviewing An Post's implementation plan for dealing with compliance issues in respect of the Accounting Direction review recommendations. ComReg will respond by separate correspondence on this.

Universal postal services specified

ComReg welcomes An Post's acknowledgement that the "Deferred Delivery" bulk mail service must be specified in accordance with the Communications Regulation (Universal Postal Service) Regulations, 2012 (SI 280 of 2012) and supporting D08/12. The Regulations state that "Deferred Delivery" means "*deposited at a delivery office for delivery within the State one day later than would otherwise be the case using the "D+n" formula.*" The Regulations further state that "delivery office" means "*an office managed by the universal postal service provider for the purposes of processing postal packets immediately prior to the activity of delivery to the addressee*". Therefore, the Regulations state that mail can be deposited in bulk at any delivery office for delivery within the state within two working days. Therefore, as stated in clearly in ComReg Decision D08/12, ComReg has specified the "Deferred Delivery" bulk mail service based on An Post's current specification of discount B in the case of letters and discount A in the case of large envelopes and packets which are offered by An Post on the basis of 350 items upwards. It is this specification that applies for the "Deferred Delivery" bulk mail service and this is clear from the Regulations and supporting Decision D08/12.

In relation to the Insured Service, ComReg again notes that it is a specified universal postal service; therefore An Post's proposed pricing for its Insured Service must be compliant with the tariff requirements of the 2011 Act.

Non-discrimination

As stated in previous correspondence and in Information Notice 12/109, ComReg will ensure that there is no pricing discrimination by An Post against any group of postal users. In particular, ComReg will ensure that any proposed discounts are supported by the cost avoided for that discount alone. In the upcoming consultation, ComReg will seek the views of respondents on this.

Cost orientation

ComReg agrees that cost orientation is as defined by section 28(1)(b) of the 2011 Act which requires that:

"prices shall be cost-oriented, that is to say, that prices shall take account of, and reflect the costs of, providing the postal service or part of the postal service concerned"

This definition does not state that prices can exceed the cost of the postal service concerned. This is logical given that for monopoly services, the major concern of any regulator is the prevention of "excessive pricing". Also,



relevant case law² indicates that the relevant "cost" in such matters is the fully allocated cost / fully distributed cost.

Further, for the avoidance of any doubt, please note that An Post must comply with all of the tariff requirements set out in the 2011 Act, including affordability. Therefore, there may be cases where prices are required to be below "cost" in order to comply with the affordability requirement and this is what ComReg meant when it stated that An Post's prices should be at or below cost.

Affordability

We note that An Post has not provided any research as to the likely reaction of its larger business and SME customers to the proposed price increases. Business customers account for over 80% of postal letter volumes. Therefore if, as a result of the proposed price increases, these customers were to cease using the postal service then this would have a major detrimental impact on the universal postal service which, absent any commensurate cost reductions, requires continued volumes in order to remain viable. Therefore, and as noted in my previous letter, a survey of An Post's business customers would have proven most useful in assessing any potential impact of a price increase on future mail volumes. However, and given An Post has not provided any research or data as to the likely reaction of its business customers, ComReg will, as part of its consultation, seek the views of An Post's business customers as to the affordability or otherwise of An Post's proposed price increases, and their likely reaction to such increases if introduced.

Terms and conditions

Again, we disagree that the terms and conditions for universal postal services is a separate task. They are linked as the terms and conditions set out the exact details of the universal postal services. This linkage is acknowledged by you in your letter of 2 November 2012. Therefore, An Post should send the proposed terms and conditions for the universal postal services as soon as possible as they are long overdue.

Financial data – Group net cash

We strongly disagree that An Post's projections for its group net cash are not a matter for ComReg and have nothing to do with ensuring the provision of the universal postal service. ComReg has been tasked with ensuring the provision of the universal postal service in the State and therefore ComReg can validly seek any information as to the current and future viability of An Post, the sole provider of that service, including information relating to An Post's financial viability.

ComReg recognises that the cash outflow includes once off investments but regardless of this ComReg remains concerned that, absent any other measures, the forecast cash position of An Post seems tight given the general

² European Court of Justice decisions in Arcor and Mobistar cases



trend in cash outflow over the past few years and in light of An Post's general working capital requirements.

Conclusion

Revenue intervention such as price increases are only a part of a solution to An Post's financial problems and only then if they do not have a significant detrimental impact on the volumes of the universal postal services. In this respect, ComReg again notes that a price increase reflective of the change in CPI since the last price increase may be appropriate as the new price cap control to be implemented will allow annual CPI changes.

ComReg considers that the most recent information provided by An Post remains lacking in certain respects, however, ComReg will nevertheless commence a public consultation on the sought after price increases before the end of 2012, subject to An Post's prompt assistance where required.

Finally, and as noted at the outset of this letter, your letter, this letter, and all other relevant correspondence and documentation will be published by ComReg in due course.

Yours sincerely

**George Merrigan,
Director, Market Framework**