Commission for
Communications Regulation

Consultation on universal postal service accounting obligations

Consultation and draft Direction

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1 Introduction

1 An Post, as the designated universal postal service provider ("USP"), is currently subject to the 2006 Accounting Direction[1] issued by the Commission for Communications Regulation ("ComReg").

2 The purpose of an accounting direction is to set out the USP's accounting obligations in respect of the universal postal service and to ensure transparency on the costing and profitability of the universal postal service. This provides ComReg with the information necessary for it to discharge its statutory functions under the Communications Regulation (Postal Services) Act 2011 ("2011 Act"). The USP's accounting obligations also enable ComReg to monitor the USP's compliance with various other obligations under the 2011 Act, including the tariff and terminal dues requirements. As per section 31(6) of the 2011 Act, the USP's accounting obligations are in addition to, and not in substitution for, the provisions of the Companies Acts relating to the preparation of statutory accounts and their audit. The Regulatory Accounts[2] are thus an additional set of accounts to meet the information requirements of ComReg and are not substitutes for the statutory accounts which An Post must prepare under the Companies Acts. The Directors of An Post remain solely responsible for the preparation and audit of those statutory accounts.

3 ComReg now proposes to give a direction to the USP pursuant to section 31 of the 2011 Act[3] (the "Proposed Accounting Direction"). The Proposed Accounting Direction, if put into effect, would replace the 2006 Accounting Direction which was established under the older statutory framework.[4]

4 This consultation sets out ComReg's preliminary views on the Proposed Accounting Direction. For the most part, ComReg proposes that the existing requirements under the 2006 Accounting Direction would continue under the Proposed Accounting Direction.

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[1] ComReg Document No. 06/63

[2] For information, An Post's Summary Regulatory Accounts (Regulatory Accounts with limited redactions for confidential information) can be found at http://www.anpost.ie/NR/rdonlyres/354DFCDE-E9F4-49C4-9435-E8F337222F2C/9086/ANPOST_SummaryRegulatoryAccounts2014.pdf

[3] Condition 31(2)(c) is in effect as ComReg is satisfied that competition in the market for postal services is not fully effective. ComReg made this opinion in Decision D13/13, dated 6 September 2013, for the purposes of enabling a price cap decision that applies for 5 years (2014 – 2019), and ComReg is also of the view that this situation is unchanged as at the present date:
"*The Commission for Communications Regulation, pursuant to section 30(2) of the Communications Regulation (Postal Services) Act 2011 ("2011 Act"), is of the opinion that the universal postal services specified in the Communications Regulation (Universal Postal Service) Regulations, 2012 (S.I. 280 of 2012) constitute a separate market and that there is no effective competition in that market*…"

[4] The European Communities (Postal Services) Regulations 2002 (S.I. 616/2002) and the European Communities (Postal Services) (Amendment) Regulations 2008 (S.I. 135/2008).

5 However, ComReg also proposes that certain additional information be included in the Regulatory Accounts, in order to enable ComReg and the USP to discharge their respective obligations under the 2011 Act. Where ComReg proposes that any additional information be provided by the USP, ComReg has considered whether the proposal is proportionate and has endeavoured to ensure that such additional information requirements could be implemented by the USP, at no or at minimal additional cost, noting that such information, as far as ComReg is aware, is already produced by the USP's current cost accounting system / other information systems, in full or in large part.

2 Executive Summary

6 Section 31 of the 2011 Act provides that ComReg may give a direction to the USP, requiring it to keep separate accounts for each of its postal services, to include distinguishing between those services which are part of the universal postal service and those which are not, where ComReg is satisfied that competition in the market for postal services is not fully effective.

7 In Document 13/82 (D13/13), ComReg formed the opinion that the universal postal services specified in the Communications Regulation (Universal Postal Service) Regulations, 2012[5] constitute a separate market and that there is no effective competition in that market. ComReg is also of the view that this situation is unchanged as at the present date[6].

8 The USP is currently subject to the 2006 Accounting Direction, which issued under the older statutory framework which was revoked and replaced by the 2011 Act. ComReg considers that it is now appropriate to review the 2006 Accounting Direction and to replace it with the Proposed Accounting Direction which would issue under section 31 of the 2011 Act. The Proposed Accounting Direction would be very similar to the 2006 Accounting Direction as to its overall purpose and effect though ComReg proposes to update and refine it in certain parts, as described herein.

9 In this document, ComReg sets outs its preliminary views on its Proposed Accounting Direction. In forming its preliminary views ComReg has considered all relevant material, including:

- The 2006 Accounting Direction;
- ComReg's Accounting Direction in telecoms and broadcasting;
- Pre-consultation engagement with, and submissions by[7], the USP; and
- Recommendations by Frontier Economics (Document No. 15/135a) and the draft Regulatory Account schedules prepared by Frontier Economics (Document Nos. 15/135b and 15/135c).

[5] S.I. 280 of 2012
[6] If effective competition were to be found, this would likely mean that such postal service should not be a postal service such that ComReg should amend its specification of the universal postal service made in Communications Regulation (Universal Postal Service) Regulations, 2012 (S.I. 280 of 2012)
[7] For information, non-confidential pre-consultation submissions by the USP are published as Document Nos. 15/135d, 15/135e, 15/135f. ComReg has considered these pre-consultation submissions by the USP.

2.1 ComReg's preliminary views for the Proposed Accounting Direction

10 For the most part, the preliminary views that follow support the continuation of the existing requirements under the 2006 Accounting Direction. Where ComReg proposes to refine or improve the 2006 Accounting Direction in some manner, ComReg has considered whether the proposal is proportionate and whether such a refinement or improvement could easily be implemented by the USP, at no or at minimal additional cost.

11 The current draft version of the Proposed Accounting Direction is set out in chapter 6. In summary, it would provide for the following:

- to maintain the current requirement that the USP provide a set of Regulatory Accounts (confidential to ComReg) from which a summary set of accounts with redactions will be extracted for publication;
- to maintain the current requirement in relation to volume and revenue recording;
- to reduce the current requirement for a reconciliation between revenue-derived volumes and operational counted volumes from an at service level to a less detailed level, namely at format level (i.e. letter, large envelope, packet, parcel) and to continue the requirement that the USP provides commentary explaining the difference between the revenue-derived and operational-based volume figures;
- to maintain the current requirements in respect of cost allocation;
- to maintain the current requirement that detailed information on the USP's process to identify avoidable, variable and fixed costs is included in the USP's Accounting Manual but to now also include worked examples of each cost category;
- to maintain the current requirement that the Real Mail Study ("RMS") be audited by an independent auditor appointed by ComReg;
- to maintain the current requirements in respect of cost identification;
- to strengthen the current requirement that cost allocation drivers are reviewed, updated and verified;

- to maintain the current requirement that the USP provides cost detail for each price point for each universal postal service (noting that is now a statutory requirement under section 28(1) of the 2011 Act);
- to maintain the current requirements with regard to inter-company and inter-segment charges and to strengthen these requirements by also requiring (a) that the source of inter-segment revenue be reported in a matrix form, and (b) that the nature and detail of all inter-company and inter-segment charges are audited by the Regulatory Auditor;
- to require the USP to report its Balance Sheet to ComReg quarterly until its cash position reaches a sufficient level (minimum of €100m[8]);
- to require improved reporting by the USP on its:
    - capital expenditure; and
    - payroll expenditure;
- to continue to require the audit to be conducted on a "present fairly" basis and to improve the definition of the scope of the annual audit to be conducted by the Regulatory Auditor, to include:
    - the Regulatory Accounts and the Accounting Manual;
    - the revenue, costs, and volumes included in the Regulatory Accounts;
    - the reconciliation between the Regulatory Accounts and the statutory accounts;
    - correctness of figures, including operational volumes and the reconciliation of revenue-derived volumes to operational volumes;
    - methodologies used regarding amortisation, cost capitalisation, and cost allocation (including transfer charges / inter-segment charges);
    - appropriateness of the usage of the cost drivers;
    - nature and detail of all transfer charges / inter-segment charges;
    - the frequency of updates used for cost allocation purposes;

[8] c.€40m at end of 2014 for An Post Company as per An Post's audited Annual Report

  - appropriateness of any changes in the cost allocation methodology; and
  - whether the Accounting Manual continues to fairly present the USP’s processes, procedures, and policies in preparing the Regulatory Accounts.

- to specify that ComReg shall appoint the Regulatory Auditor;
- to specify that the USP’s Accounting Manual shall no longer be approved by ComReg;
- to continue to not require the USP to publish its Accounting Manual but rather include sufficient detail on the accounting principles and basis of preparation in the Regulatory Accounts and the Summary Regulatory Accounts;
- to require improved information in relation to mail volumes, by requiring:
  - reconciliations by format between operational mail volumes recorded at the DSU and Mail Centre level to be included in the USP's Regulatory Accounts (to give ComReg added assurances as to the accuracy of the USP's volume counts);
  - that the reconciliation of the USP’s revenue-derived and operational-based mail volumes be audited by the Regulatory Auditor;
  - the USP to include in its Accounting Manual details as to how its operational-based mail volumes are calculated, including the process for validating machine counts (as machine counts account for the vast majority of operational volumes) and the degree of accuracy to which machines are tested (to increase confidence and to ensure accuracy in the machine counts which will be used as a check against the revenue-derived volumes);
  - the USP to include in its Accounting Manual details of the process for reviewing manual counts (which only account for a small amount of operational volumes), in particular, average container fills; review average container fills every quarter; and report the results of the average container fill reviews in its Accounting Manual.

12 A draft Regulatory Accounts schedule has been developed in order to minimise ambiguity with regard to the Regulatory Accounts' content, format, and the level of detail that is required. The schedule includes required areas of commentary to help ensure sufficient commentary is provided. The proposed Regulatory Accounts is set out in Document No. 15/135b and the proposed Summary Regulatory Accounts (to be published by An Post) is set out in Document No. 15/135c. For information, Regulatory Accounts proposed by the USP are set out in Document Nos. 15/135d (confidential to ComReg) and 15/135e (to be published by An Post); ComReg has considered this pre-consultation submission by the USP.

13 As stated in ComReg's Consultation guidelines, the purpose of a public consultation is to allow ComReg to consider the views of interested parties in reaching a decision. In making any final decisions in this matter, ComReg will consider the information, evidence, and views submitted by all respondents to this consultation while also having regard to any other relevant information and evidence before it.

3 Background

14 As noted previously by ComReg[9], the USP is facing significant ongoing financial challenges, largely due to the significant decline in traditional mail volumes in recent years and its deteriorating cash position and high cash outflow rate.

15 Given these challenges, and in order to discharge its statutory objectives and functions, ComReg relies on information gathered contained in the Regulatory Accounts, currently produced pursuant to the 2006 Accounting Direction. Information from the Regulatory Accounts is critically important to ComReg.

3.1 Legal and Regulatory

16 An Post, the sole designated USP in the State, is currently subject to the 2006 Accounting Direction. The 2011 Act has since been enacted, in August 2011, and amongst other things it transposes the "Postal Directive" into Irish law.[10]

17 Therefore all references in this document to provisions of the 2011 Act should be inferred as also referencing the corresponding provision(s) of the Postal Directive, unless otherwise stated.

18 In addition, all references in this document to "section(s)" are references to "section(s) of the 2011", unless otherwise stated.

3.1.1 2011 Act

19 The 2011 Act sets out ComReg's statutory objectives in relation to the provision of postal services are:

- 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;
- to promote the interests of postal service users within the Community; and
- to facilitate the development of competition and innovation in the market for postal service provision.

[9] See ComReg Document Nos. 14/59, 13/21, 12/138
[10] Directive" 97/67/EC of the European Parliament and of the Council of 15 December 1997 ("Postal Directive"), as amended by subsequent Directives in 2002 and 2008, which was transposed into Irish Law by the 2011 Act.

20 Section 31 empowers ComReg to give a direction to the USP requiring it to keep, in its internal accounting system, separate accounts for each service it provides. The provision of robust accounting data by the USP is essential to ensure that ComReg and the USP can meet their respective obligations under the 2011 Act, which include the following:

- ensuring compliance with section 31 - universal postal service accounting obligations;[11]
- ensuring compliance with section 28 - tariff requirements in relation to cost-orientation and non-discrimination;
- ensuring compliance with section 29 - that intra-Community (i.e. between European member states) terminal dues agreements are fixed in relation to the costs of processing and delivering incoming cross-border mail and are non-discriminatory;
- ensuring that adequate information is available for monitoring compliance with the price cap (section 30) and for setting future price caps;
- ensuring compliance with section 33 concerning access to the postal network of the USP, and in particular section 33(7) which may require ComReg to make pricing decisions in relation to such access; and
- assessing any application made by the USP under section 35, seeking funding in relation to what it submits are the net costs of providing the universal postal services.

Further details on each of the above provisions are provided below.

Section 31 – ComReg's power to issue an Accounting Direction

21 ComReg can give a direction under section 31(1) if any or all of the conditions specified in section 31(2) are met. These include, at section 31(2)(c), that ComReg is satisfied that competition in the market for postal services is not fully effective. ComReg made a opinion to this effect in Decision D13/13 dated 6 September 2013, pursuant to section 30(2) of the 2011 Act, for the purposes of enabling a price cap decision that applies for 5 years[12]:

[11] Article 14 of the Postal Directive requires that Member States shall take the measures necessary to ensure that the accounting of the universal service providers is conducted in accordance with the provisions of Article 14 of the Postal Directive. Article 14 of the Postal Directive goes on to set out the requirements which universal service providers must meet in relation to the keeping of accounts. Article 14 of the Postal Directive also sets out the criteria which a universal service provider must meet in relation to the allocation of costs.

[12] Section 30(4) of the 2011 Act.

"*The Commission for Communications Regulation, pursuant to section 30(2) of the Communications Regulation (Postal Services) Act 2011 ("2011 Act"), is of the opinion that the universal postal services specified in the Communications Regulation (Universal Postal Service) Regulations, 2012 (S.I. 280 of 2012) constitute a separate market and that there is no effective competition in that market…*

This Opinion shall remain in force until further notice."

22 That remains ComReg's opinion – i.e. that the specified universal postal services constitute a separate market in which there is no effective competition. If this situation was to change and if ComReg should form the opinion that certain specified universal postal services do face effective competition in the State, then ComReg would propose revising its specification of the universal postal service by removing such postal services from that specification, on the basis that they were being offered to postal service users in an open market in which there is effective competition and therefore no longer require to be universal postal services.

23 Any future direction to the USP under section 31 would require the USP, in its internal accounting systems, to keep separate accounts for each service it provides which is:

- part of the universal postal service, and
- not part of the universal postal service.

24 Pursuant to section 31(3), such a direction would also provide for:

- rules relating to the identification of costs;
- rules relating to the allocation of costs;
- rules relating to the use of internal cost accounting systems;
- the verification by a statutory auditor of compliance with internal cost accounting systems;
- the publication of such accounts and other information as ComReg considers appropriate (subject to the protection of any information which ComReg considers confidential);
- the publication of a statement of compliance with section 31 and ComReg's Direction; and
- such other matters relating to the requirements of section 31 and ComReg's Direction as ComReg considers appropriate.

25 Section 31(4) requires ComReg to keep available, to an adequate level of detail, information on the cost accounting systems applied by a USP, and to submit such information to the European Commission on request.

26 Section 31(5) further requires that the USP shall make available in confidence to the European Commission, on request, detailed accounting information arising from its cost accounting systems.

27 In addition to the provision of section 31 as outlined above, ComReg would note that an appropriately dis-aggregated set of Regulatory Accounts is an essential input to ensuring compliance with sections 28, 29, 30, 33 and 35.

Section 28 – tariff requirements

28 The USP's tariffs for its universal postal services must comply with certain requirements set out in section 28. In summary, such tariffs must be affordable, cost-oriented, uniform, transparent, and non-discriminatory.

29 The requirement that such tariffs be cost-oriented means that they must take account of and reflect the costs of providing the particular postal service or part of the postal service. To ensure that this is done, it is essential that the USP has robust cost data available to it in relation to each of its universal postal services. ComReg also requires such data in order to monitor compliance.

Section 29 – terminal dues

30 Under section 29, the USP must ensure that its agreements on terminal dues for intra-community cross-border mail comply with the following requirements:

- terminal dues shall be fixed in relation to the costs of processing and delivering incoming cross-border mail;
- levels of remuneration shall be related to the quality of service achieved; and
- terminal dues shall be transparent and non-discriminatory.

31 In order to comply with the cost and non-discrimination requirements, it is essential that the USP has robust cost data available to it in relation to the costs of processing and delivering incoming intra-community cross-border mail. ComReg also requires such data in order to monitor compliance.

Section 30 – price cap

32 Section 30 relates to setting a price cap for certain universal postal services provided by the USP. In order to comply with section 30, it is essential that An Post is able to accurately determine the costs incurred by it in relation to providing those universal postal services, and only those universal postal services, that are included within the scope of the price control. Also, as mail volumes were an important input in setting the current 5-year price cap (June 2014 - June 2019), it is essential that the USP is able to accurately determine its actual mail volumes to ensure that the universal postal service remains sustainable and at an affordable price for the benefit of all postal service users.

Section 33 – access to the USP's postal network

33 Section 33 relates to access to the USP's postal network. Under section 33, a postal service provider has the right to enter into negotiations with the USP with a view to concluding an agreement to gain access to the USP's postal network. Such a provider may also serve notice on ComReg upon the commencement of any such negotiations. Pursuant to section 33(3), where agreement has not been reached within the period specified by ComReg, ComReg shall take such steps as are necessary to resolve the dispute. Pursuant to section 33(7), in making a decision in relation to a dispute on access, ComReg may impose or amend conditions relating to access to a USP's postal network and such conditions may include -

- the price of access,
- terms and conditions relating to matters other than price, and
- rules for the separation of accounts relating to access to the postal network.

34 In order to meet its obligations under section 33, it is essential that ComReg has access to robust accounting data relating to the costs (and particularly avoided costs) of providing access to the USP's postal network.

Section 35 – net cost of provision of universal postal service

35 Section 35 relates to the net cost of provision of universal postal services and, in particular, to any application by the USP for funding of the net costs (if any) of providing a universal postal service. In order for ComReg to be in a position to assess any such application, it is critical that robust accounting information relating to the costs of provision of the universal postal service is available[13].

[13] ComReg has set out the requirements of any net cost application by the USP in D09/13 dated 25 July 2013.

3.1.2 Postal Directive

36 Article 14 of the Postal Directive, which concerns accounting by the USP, requires that:

- there are separate accounts within the internal accounting system in order to clearly distinguish between each of the services which are part of the universal service and those which are not;
- this accounting separation shall be used as an input to calculate the net cost of the universal postal service; and
- such internal accounting systems shall operate on the basis of consistently applied and objectively justifiable cost accounting principles.

37 With respect to the cost allocation process, Article 14 requires that:

- costs which can be directly assigned to a particular service or service shall be so assigned;
- common costs, that is costs which cannot be directly assigned to a particular service or service, shall be allocated as follows:
    - whenever possible, common costs shall be allocated on the basis of direct analysis of the origin of the costs themselves;
    - when direct analysis is not possible, common cost categories shall be allocated on the basis of an indirect linkage to another cost category or group of cost categories for which a direct assignment or allocation is possible, the indirect linkage shall be based on comparable cost structures;
    - when neither direct nor indirect measures of cost allocation can be found, the cost category shall be allocated on the basis of a general allocator computed by using the ratio of all expenses directly or indirectly assigned or allocated, on the one hand, to each of the universal services and, on the other hand, to the other services; and
    - common costs, which are necessary for the provision of both universal postal services and non-universal postal services, shall be allocated appropriately; the same cost drivers[14] must be applied to both universal postal services and non-universal postal services.

[14] Cost driver is an event or factor that has a systematic relationship to a particular type of cost and which causes that cost to be incurred

3.2 Overview of how USP prepares Regulatory Accounts to meet 2006 Accounting Direction

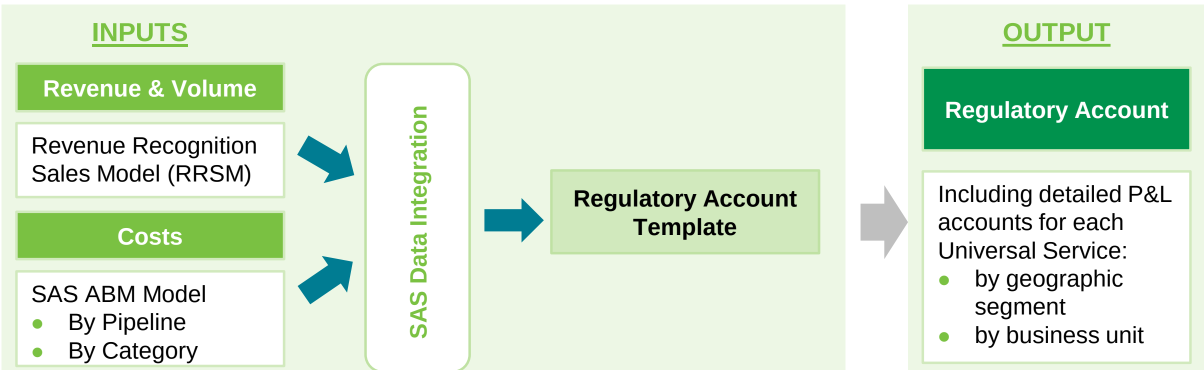
38 As background, below is an overview of how the USP currently prepares its Regulatory Accounts to meet ComReg's requirements as set out in the 2006 Accounting Direction.

39 The Regulatory Accounts are based on the USP's financial records and are reconciled to the operating profit and the Balance Sheet as reported in the USP's Statutory Accounts. The Regulatory Accounts are prepared in accordance with the same accounting policies as the USP's Statutory Accounts, unless otherwise stated. The Regulatory Accounts are prepared adopting the following:

- Procedures and policies as documented in the Accounting Manual, which reflects the requirements of the 2006 Accounting Direction; and
- Accounting Policies for the Profit and Loss statements are consistent with Irish GAAP as applied in the An Post Statutory Accounts.

40 The inputs, processes and output of the Regulatory Accounts can be represented graphically as follows:

Figure 1: Inputs, processes, and output of the Regulatory Accounts



Source: An Post's Accounting Manual

3.2.1 Basis of preparation of the Regulatory Accounts

General principles

41 The Profit and Loss Statements by service are prepared by applying activity based costing ("ABC") methods and principles in order to allocate costs. The resulting statements present the fully allocated costs of services.

42 Costs are directly assigned to services as far as practicable. Common operational costs that cannot be directly assigned are instead attributed to services using appropriate cost drivers, in line with the 2006 Accounting Direction. Where no appropriate cost driver is identified, costs are allocated to services using a general allocator, that is, an Equi-Proportionate Mark-Up ("EPMU").

Revenue

43 Revenue is assigned directly to the appropriate service, with the exception of stamp and meter revenue. Stamp and meter revenue is assigned to services by applying a statistical analysis of mail stream characteristics (the "Real Mail Study"), including the use of observed tariffs. The revenue from value-added services is calculated using the mail volumes recorded by the USP's Track and Trace system.

44 Postage income is recognised as sales are made, with an adjustment for stamps sold and unused, and balances in postage meter machines unused at year end.

Volumes

45 Mail volumes are a key driver in allocating costs.

46 Mail traffic volumes for domestic and outbound international stamped and metered mail are measured using a revenue-derived traffic methodology, based on reported revenues and mail sampling.

47 Mail traffic volumes for non-stamped (e.g. Bulk mail) and metered mail are primarily measured from the USP's billing or Track and Trace systems.

48 Mail traffic volumes for inbound international mail are measured by the USP's International Mail System ("IMS").

Operating costs

49 For the purposes of the Regulatory Accounts, pay and non-pay costs are separately identified and within each heading are further categorised between Revenue Collection, Collection, Outward Sorting, Transport, Inward Sorting, and Preparation and Delivery.

50 For pay costs, the hours worked by operational staff of the USP in performing their daily duties are recorded by work activity in a database that reconciles to the payroll system. This facilitates pay costs to be assigned to activities based on the time spent by staff on specific activities.

51 Other costs are assigned to activities by the use of appropriate cost drivers.

4 Universal postal service accounting obligations

52 This chapter sets out ComReg's preliminary views regarding the proposed universal postal service accounting obligations to be set out in the Proposed Accounting Direction. In forming these preliminary views ComReg has considered all relevant material, including but not limited to:

- The 2006 Accounting Direction[15];
- The current Regulatory Accounts (format, content, level of detail, detail currently published)[16];
- The USP's Accounting Manual[17];
- ComReg's Accounting Direction in fixed telecoms[18] and in broadcasting transmission[19];
- Studies and references, including:
    - The European Regulators Group for Postal Services ("ERGP") Common Position on Cost Allocation rules[20]
    - Recommendations on best Practice for Cost Accounting Rules III[21]
    - Report by Analysys Mason on 'Review and assessment of USP's compliance with the Accounting Direction'[22];
- Pre-consultation engagement with and submissions by the USP[17];
- Recommendations made by Frontier Economics (Document No.15/135a) and proposed Regulatory Account templates (Document No. 15/135b and 15/135c).

[15] ComReg Document No. 06/63 @ http://www.comreg.ie/_fileupload/publications/ComReg0663.pdf
[16] Non-confidential version @ http://www.anpost.ie/NR/rdonlyres/354DFCDE-E9F4-49C4-9435-E8F337222F2C/9086/ANPOST_SummaryRegulatoryAccounts2014.pdf
[17] Confidential. For information, non-confidential pre-consultation submissions by the USP can be found at ComReg Document Nos. 15/135d, 15/135e, 15/135f.
[18] ComReg D08/10 (http://www.comreg.ie/_fileupload/publications/ComReg1067.pdf). See also Eircom's separated accounts at http://www.eircom.net/regulatoryinformation/separated-accounts/
[19] ComReg Document No. 13/71 (http://www.comreg.ie/_fileupload/publications/ComReg1371.pdf).
[20] http://ec.europa.eu/internal_market/ergp/docs/documentation/2012/ergp-12-28rev1-common-position-on-cost-allocation-rules_en.pdf
[21] http://www.cept.org/files/1049/documents/List%20of%20documents%20(history)/CERP%20Recommendation%20on%20best%20Practices%20for%20Cost%20Accounting%20Rules%20III.pdf
[22] October 2012 – confidential.

53 The preliminary views that follow are, for the most part, consistent with those which led to the 2006 Accounting Direction. Where ComReg proposes refinement or improvement for the Proposed Accounting Direction, such that it would differ in some material respect from the 2006 Accounting Direction, ComReg has considered whether such refinement or improvement is proportionate and whether it could easily be implemented by the USP, at no or at minimal additional cost. In the draft Regulatory Impact Assessment ("RIA") in Chapter 5, ComReg has set out why it considers that its proposed refinements / improvements are the best options.

54 ComReg's preliminary views on the USP's accounting obligations are examined under the following headings:

(1) Measuring mail volumes and revenues

(2) Cost identification and allocation

(3) Regulatory reporting

(4) Compliance requirements

(5) Timetable to comply with Direction

(6) Format of the Regulatory Accounts.

4.1 Measuring mail volumes and revenues

55 Mail traffic (i.e. volume and number of postal packets) is one of the major cost drivers in ABC costing for postal services. It is directly used to attribute direct costs and to allocate joint costs. It is therefore necessary to ensure that mail traffic is measured accurately, before considering cost allocation. For this reason, the current 2006 Accounting Direction put in place rules relating to measuring mail traffic and allocating revenues. An overview of the current rules is set out below followed by a preliminary consideration as to whether the current rules are sufficient to be carried over in the Proposed Accounting Direction or whether certain improvements should be made, particularly in relation to improved reconciliations and documentation.

4.1.1 Accounting Direction rules for measuring mail volumes and revenues

56 There are two main methods for calculating mail volumes:

(1) Revenue-derived volumes: these volume figures are derived by dividing the total revenue collected for the postal packet in question by the average observed unit price of that postal packet (derived using a sampling exercise).

(2) Operational-based volumes: these volume figures are based on machine counts or, where volume cannot be counted by machine, by estimating the total number of containers (e.g. trays and bags) of the postal packet in question and multiplying that figure by the average fill of a container.

57 The USP's Accounting Manual sets out, at a high level, the USP's approach to measuring volumes and revenue to meet the requirements of the 2006 Accounting Direction made by ComReg.

58 The USP's primary method for allocating revenues to particular services is its Revenue Recognition Sales Model ("RRSM"). The RRSM is used to calculate the revenue-derived volume by service and is divided into three main areas, namely:

(1) domestic and international outbound mail;

(2) international inbound mail; and

(3) value added services.

59 The 2006 Accounting Direction requires that revenue, by service, shall be recorded at the point of sale. It also requires that where revenue recorded at the point of sale cannot be assigned to a particular service, it shall be apportioned to services on the basis of statistical sampling, known as the Real Mail Study[23] ("RMS") (accurate to +/-1% at the 95% confidence level).

4.1.1.1 Domestic and international outbound mail

60 The USP's Accounting Manual states that stamped and metered volumes for Domestic and International Outbound postal packets are primarily determined by applying data from the RMS. The exception is where the USP's internal systems provide more exact data (such as registered mail and the use of point of sale equipment at An Post's post offices which captures sales information). For bulk mail, the USP's Integrated Financial System ("IFS") is used to record sales and data is captured on postings by service, destination, and weight step, based on dockets provided by bulk mail customers.

[23] The USP conducts a Real Mail Study (RMS) on a continuous basis throughout each year. The requirements of the RMS are set out by the CEN Standard EN13850:2012. Real mail flows are sampled as they move through the USP's network and information on these postal packets is then collected and audited. The sample is then used to create a mail profile for the USP mail flows, which is applied to:

- mail volumes and revenue recorded at the point of sale that cannot be directly assigned to their use for specific services or retention by users for later use (e.g. stamps and franking machine credits); and
- mail services recorded in the outward phase of the postal pipeline, which cannot be assigned to their specific services (e.g. manually sorted postal packets).

The RMS is audited by an auditor appointed by ComReg.

61 Stamped, metered and bulk mail sales are adjusted for various factors in order to derive a total revenue figure for Domestic and International Outbound postal packets. That figure is then divided between the various services using the RMS volume profiles, with service-level revenue assigned to weight steps using RMS weight profiles. The revenue for each weight step is divided by the observed tariff for that type of mail, in order to calculate the revenue-derived volumes.

62 Clearly, the results of the RMS are a key input into accurate service-level revenue recording. The RMS is audited annually in accordance with section 5.2(c) of the 2006 Accounting Direction, by an independent auditor appointed by ComReg. The audit includes an assessment of the RMS sample design, implementation and results.

4.1.1.2 International inbound mail

63 The USP's revenues for International Inbound mail (or "Terminal Dues") are the payments it receives from Postal Administrations in other jurisdictions, for sorting, transporting and delivering in the State mail which it receives from them. The payment rates for Terminal Dues can be set by various means:

(1) Universal Postal Union ("UPU") rates apply to non-EU Member States. These are multi-lateral rates.

(2) REIMS rates apply to EU Member States which have signed up to REIMS. These are multi-lateral rates.

(3) Bi-lateral commercial agreements. Based on its Accounting Manual, it is understood that the USP has bilateral agreements with ✂.

64 The USP's revenues for International Inbound mail are thus calculated by reference to its various Terminal Dues agreements with operators in other jurisdictions (whether they be UPU, REIMS, or separate bilateral agreements) and the volume recorded on its IMS.

4.1.1.3 Value added services

65 Revenue from value-added services are captured in large part direct from the USP's sales systems. Table 1 below sets out a high level summary of how revenue from value-added services are captured and incorporated by the USP into its RRSM model.

Table 1. Value-added services revenue measurement

	Volume source	Revenue calculation method
Registered	Track & Trace[24]	Two elements: **Registered Fee** revenue is calculated using sampling to allocate volumes. **Postage fee** revenue is calculated from the weight profiles in the counter Automation system and sampling.
Express Post	Track & Trace[25]	Tariffs applied to volumes to calculate revenue.
Philatelic	No volumes captured or calculated	Sales recorded in IFS system. Total Philatelic revenue is deducted from Total Postage Stamp Sales.
Passport Express	Revenue and Volumes captured on the Counter Automation System, Ceadúnas Account Docket and subsequently the IFS.	
Redirections / Mail Minder	Must be paid for by cheque or credit card. These receipts are entered into IFS monthly showing the revenue associated with this.	
Business Collections	Revenue details entered into IFS.	
Private Box / Bag	Revenue details entered into IFS.	
Publicity Post	Since 2012, Publicity Post is no longer defined as a 'postal service'[26].	

Source: Frontier Economics based on USP's information

Parcels

66 The USP captures its parcels revenue primarily through its Track and Trace system. Barcodes are read as parcels pass through the system and this recorded data is then associated with customer details, set-up in the USP's IFS. Commercially invoiced revenue can then be captured direct from the accounts module of the IFS, whereas stamp/meter parcels are calculated by the average price point from the USP's Counter Automation System, multiplied by the volumes from its Track and Trace system.

[24] International Outbound volumes and volumes captured on the Counter Automation System are deducted from Track & Trace volumes and volumes related to billing customers (from IFS) are added.

[25] International Outbound volumes and volumes captured on the Counter Automation System are deducted from Track & Trace volumes and volumes related to billing customers (from IFS) are added.

[26] Consistent with SI 280 of 2012

Preliminary view on measuring mail volumes and revenues

67 As can be seen from above, the USP has different methods for measuring its mail volumes and revenues, depending on the particular service. Having considered these against international best practice[27] and recommendations by Frontier Economics, ComReg, pursuant to section 31(3)(g) of the 2011 Act, is of the preliminary view that the 2006 Accounting Direction requirements on measuring mail volumes and revenues remain appropriate and that no amendments to same are required.

68 Consequently, ComReg proposes that the current requirement - that "*the Regulatory Accounts shall contain volume information that shows mail volume, by service, recorded from revenue data recorded at the point of sale*" – should be carried over in the Proposed Accounting Direction, and that the RMS should continue to be audited by an independent auditor appointed by ComReg.

4.1.2 Reconciliation of revenue and operational mail volumes

69 The 2006 Accounting Direction requires the USP to reconcile its Revenue-derived and Operational-based mail volumes, for each postal service, and to explain any discrepancy between a Revenue-derived figure and the comparable Operational-based figure.

70 The differences between the USP's Revenue-derived and Operational–based mail volumes have been decreasing over time, as shown in Table 2 below. In 2014, Operational-based volumes were 2.1% higher than Revenue-derived volumes at a total level, but the % differences are much higher by format (% information on differences by format are currently not published by An Post).

[27] See CERP (2009) Recommendation on best Practices for Cost Accounting Rules III and ERGP (2013) Report of specific cost allocation rules

Table 2: Reconciliation of revenue derived and operational based volumes

	2012	2013	2014
Operational volume	701.6	659.6	614
Revenue derived volume	642.3	621	601.4
Difference (€m)	59.3	38.6	12.6
Difference (%)	9.2%	6.2%	2.1%

Source: Summary Regulatory Accounts

71 In its 2014 Regulatory Accounts, the USP gave two reasons for the differences between its Revenue-derived and Operational-based volumes:

(1) That sampling is undertaken to an accuracy of +/- 1%; and

(2) That assumptions are required for Operational-based volume counting (typically, using “standard fill” assumptions for containers).

72 ComReg considers that these explanations are insufficient having regard to the USP’s obligations under the 2006 Accounting Direction. ComReg must note, in this regard, that the differences between Revenue-derived and Operational-based volume figures have fluctuated significantly, year-on-year, despite the fact that the underlying methodologies have not changed (i.e. the statistical accuracy of the mail sampling has not changed and the underlying assumptions have not changed).

73 Moreover, the 2006 Accounting Direction also requires that the USP “*reconciles revenue derived volumes with operational data recorded in the outward phase of the postal pipeline, together with details of volume trends by service recorded using the two methods*”. That is, rather than reconcile mail volumes at an aggregate level, the USP is required to provide more disaggregated details of mail volumes reconciliation, by service. This requirement is in line with international best practice[28]. However, the USP does not currently do this.

74 There are merits to reconciling mail volumes by service but in its pre-consultation engagement the USP has advised ComReg that such reconciliation would, in the USP’s view, require significant additional resources. However, the USP did not provide any evidence to support this contention.

[28] CERP (2009) Recommendation on best Practices for Cost Accounting Rules III

Preliminary view

75 Having considered international best practice[29] and the recommendations of Frontier Economics, ComReg is of the preliminary view, pursuant to section 31(3)(g) of the 2011 Act, that requirements in the 2006 Accounting Direction, on reconciling Revenue-derived and Operational-based mail volumes, remain appropriate. However, having considered the USP's statement that a reconciliation at service level would require significant additional resources, and the view of Frontier Economics in respect of this, ComReg proposes to reduce the requirement of the reconciliation by service to a reconciliation at a less detailed level, namely by format (i.e. letter, large envelope, packet, parcel). ComReg considers that this proposal is proportionate, given the USP's statement on its capability to reconcile its volume by service. ComReg thus proposes that the current requirement in the 2006 Accounting Direction be amended to a less onerous requirement such that the USP "*reconciles by format revenue derived volumes with operational data recorded in the outward phase of the postal pipeline, together with details of volume trends by format recorded using the two methods*".

76 The USP currently provides the reconciliation by format, in the confidential version of the Regulatory Accounts provided to ComReg, which means that there would be no additional cost to the USP under this proposal.

4.1.3 Reconciliation of operational volume counts

77 The USP conducts mail volume checks at two levels of its operational pipeline:

(i) At the Mail Centre level, and

(ii) At the Delivery Service Unit ("DSU") level,

78 To enable Frontier Economics to conduct its review, the USP provided documentation which set out the key steps by which Daily Volume Mail reports are completed, at each of its four Mail Centres. The USP also provided detail on the pre-advice notifications received by DSUs on the volumes despatched from Mail Centres and that DSU volumes received are recorded on the Mails Performance Management System ("MPMS").

79 Given the information available to the USP, it should not be difficult for the USP to reconcile its comparable mail volume figures resulting from counts conducted at the level of the DSU and the Mail Centre. However, the USP does not currently seek to reconcile these respective mail volume figures.

[29] See CERP (2009) Recommendation on best Practices for Cost Accounting Rules III and ERGP (2013) Report of specific cost allocation rules

80 Frontier Economics recommends that the USP's operational mail volumes, recorded at DSU and Mail Centre level, should be reconciled by the USP and included in its Regulatory Accounts, to give added assurance as to the accuracy of the USP's mail volume counts. Frontier Economics further recommends that this reconciliation should be done by format (i.e. letter, large envelope, packet, and parcel) in order that the USP can identify and explain any divergences as may occur.

Preliminary view

81 ComReg agrees with the above recommendations and is of the preliminary view that the Proposed Accounting Direction, pursuant to section 31(3)(g) of the 2011 Act, should require the USP to reconcile quarterly its Mail Centre and DSU mail volumes, by format. This should not be onerous on the USP and is a matter of more detailed reporting. This reconciliation would be included in the supplementary schedule of volume reconciliation in the Regulatory Accounts. This requirement should ensure that the volume information in the Regulatory Accounts is robust. This is of particular importance given that volume declines are somewhat outside the control of the USP. Also, it is critical to know actual volume declines as if actual volume declines should significantly exceed the USP's forecast declines, as provided by the USP for the price cap decision, then this could have an adverse effect on the provision of the universal postal service where such actual volume declines are outside the control of the USP.

4.1.4 Audit of the reconciliation with operational based volumes

82 Although the USP currently does reconcile its Revenue-derived and Operational-based mail volume figures, this reconciliation is not currently audited by an independent auditor.

83 Frontier Economics examined whether auditors typically audit volume reconciliations. Frontier Economics noted that the ERGP[30] states that reconciliation between volume measurements is completed in 60% of the countries in its 2013 study, with 36% of the countries including an independent audit of the reconciliation in their regulatory accounts.

84 ComReg considers that if the USP's reconciliations were audited then this would give added assurance that its volume measurements were accurate over time. This would be of benefit to both ComReg and the USP. Again, if actual volume declines should significantly exceed the USP's forecast declines, as provided by the USP for the price cap decision, then this could have an adverse effect on the provision of the universal postal service where such actual volume declines are outside the control of the USP.

[30] ERGP (2013), Report on specific cost allocation issues

85 Furthermore, this is particularly important because there is, at present, relatively little information in the Regulatory Accounts as to the reasons for the divergence between Revenue-derived and Operational-based volumes and mail volumes are a critical component for driving and allocating cost in the USP's internal cost accounting system.

Preliminary view

86 For the reasons set out above and having considered international best practice and the recommendations of Frontier Economics, ComReg is of the preliminary view that the Proposed Accounting Direction would, pursuant to section 31(3)(g) of the 2011 Act, specify that the USP's Revenue-derived and Operational-based mail volume reconciliations shall be audited by the Regulatory Auditor.

4.1.5 Reporting the process for measuring Operational based volumes and their accuracy

87 Frontier Economics considered:

(1) the extent to which the USP transparently records its methods for measuring Operational-based volumes, and

(2) whether the USP's methods yield accurate mail volumes estimates.

88 The USP measures its Operational-based mail volumes from a combination of machine counts and (where machine counts are not feasible) manual counts of postal packets. According to the USP, nearly all (✂%) of its Operational-based volumes are measured from its machine counts while very little (✂%) are measured from its manual counts.

Automated machine counts

89 Machine counts make up a large proportion of the mail volume count and it is therefore important to ensure that these counts are accurate.

90 There is little information in the USP's Accounting Manual as to how it ensures that its machine counts are sufficiently accurate. Frontier Economics therefore asked the USP to provide documentation and details of the mechanisms or controls by which it ensures that its mail volume counts are accurate, as the mail passes through the Mail Centre pipeline (including handover between different pipeline stages, into and out of the Mail Centres).

91 In response, An Post stated that it conducts a daily "pre-flight" testing of each machine before it commences live mail processing, which testing procedure is documented. An Post also stated that if a pre-flight inspection uncovers a problem then maintenance work commences to correct the problem.

92 However, Frontier Economics noted that the degree of accuracy to which the machines are tested is not recorded. The degree of accuracy should be recorded as it would increase confidence in the results of the machine counts.

Preliminary view

93 Having considered the recommendation of Frontier Economics, ComReg is of the preliminary view that the Proposed Accounting Direction should, pursuant to section 31(3)(g) of the 2011 Act, include details as to how Operational-based volumes are to be calculated (given that machine counts account for the vast majority of Operational-based volumes). This would include specifying the process for validating machine counts and the degree of accuracy to which machines would be tested, in order to ensure accuracy and thereby increase confidence in the machine counts. This information would be used as a check against the Revenue-derived volumes.

Manual counts

94 Manual count figures are measured by counting the number of containers of non-machinable postal packets and multiplying the number of containers by the average quantity of postal packets per container ("average container fill"). Therefore, assumptions as to the average container fill are a key input to a manual count. Again, there is currently minimal detail in the USP's Accounting Manual as to what these assumptions are or how they are arrived at.

95 Although manual counts make up a small amount (✂%) of Operational-based volumes, they are nonetheless very important as regards large packets and parcels, which currently cannot be counted by machines and so must be counted manually. It is thus important to ensure that the manual counting process is carried out properly, in order that the resulting volume figures can be relied on and reconciled with the Revenue-derived volumes.

96 ComReg must note in this regard that the USP appears to apply a number (✂) of assumptions as to average container fills, at its DSUs, but appears to classify its mail in a more disaggregated fashion and to apply a higher number (✂) of significantly different assumptions for average container fills, at its Mail Centres.

97 Regarding the process for reviewing average container fills, the USP has stated that this is done once a year by the Head of Mails Processing and that any changes to the existing figures must be approved by the Mails Operations Director. The USP's Accounting Manual currently provides no details of these reviews.

98 However, Frontier Economics has noted that the average container fill assumptions have not changed since 2012, despite the fact that the postal sector period has seen significant change since then.

99 Frontier Economics therefore recommend that average container fill assumptions should be reviewed quarterly rather than annually, as quarterly reviews could take account of seasonal changes and any variations in mail characteristics which could impact on assumptions as to average container fills. This should improve the accuracy of the manual counts and yield more robust and reliable results.

Preliminary view

100 ComReg notes and agrees with Frontiers Economics recommendation and is therefore of the preliminary view that the Proposed Accounting Direction should, pursuant to section 31(3)(g) of the 2011 Act, require the USP to:

- include in its Accounting Manual details of the process for reviewing average container fills;
- review average container fills every quarter; and
- report the results of the average container fill reviews in its Accounting Manual.

101 This requirement should improve the accuracy of manual counts, which are important for the reasons set out above.

4.2 Cost Identification and Allocation

102 Sections 31(3)(a) & (b) of the 2011 Act requires that any accounting direction given by ComReg to the USP shall provide for (a) rules relating to the identification of costs, and (b) rules relating to the allocation of costs.

103 The 2006 Accounting Direction (issued under the previous statutory framework) sets the following rules in respect of cost identification and allocation:

- The Accounting Manual shall set out how the operating cost of the various aspects of the public postal network are identified.
- The Accounting Manual shall set out the basis on which the costs of particular activities are to be apportioned between services. Costs shall be apportioned between the various services that use each aspect of the network on the basis of factors/drivers which reflect the different impact of each postal packet on the cost of the activity.

4.2.1 Identification of costs

104 The 2006 Accounting Direction requires the USP's Accounting Manual to provide "*the process by which USP identifies how avoidable, variable and fixed costs are defined*".

105 The USP's Accounting Manual states that fixed costs are those that do not fluctuate with changes in volumes, whereas variable costs are those that do change with changes in volumes. While these are useful definitions, they provide little clarity as to how each type of cost is actually identified in the regulatory accounts process.

106 The USP's Accounting Manual also contains no detail on the process by which the USP identifies avoidable costs. This is in stark contrast to the significant level of detail contained in Royal Mail's equivalent document[31], extracts of which are reproduced in Frontier Economics' report.

107 ComReg may require details of how the USP identifies avoidable costs to carry out certain functions. For example, section 31 of the 2011 Act requires that ComReg may, in certain circumstances, have to resolve any dispute as may arise between the USP and another postal service provider that seeks access to the USP's network. If any such dispute should involve having to set a price for access then that could require involve ComReg having to consider the USP's avoidable costs (such as costs it would avoid by granting access to another postal service provider). Avoidable costs would also need to be known if the USP should ever seek funding for what it submitted was the net cost of providing a universal postal service, pursuant to section 35 of the 2011 Act. In such circumstances, ComReg would have to assess any net costs that the USP would avoid if it did not have to provide a universal postal service.

Preliminary view

108 ComReg, having considered the recommendation of Frontier Economics, is of the preliminary view that the existing requirements of the 2006 Accounting Direction – requiring the USP to provide details of the processes by which it identifies avoidable, variable, and fixed costs - should be carried over in the Proposed Accounting Direction pursuant to section 31(3)(a) of the 2011 Act, in order to ensure that ComReg can exercise its various functions under the 2011 Act, as required.

4.2.2 The allocation of the cost activities (direct, indirect or common)

109 The 2006 Accounting Direction, consistent with Article 14 of the Postal Services Directive, requires costs to be allocated as follows:

- costs which can be directly assigned to a particular service shall be so assigned;
- common costs, which are costs that cannot be directly assigned to a particular service, shall be allocated as follows:

[31] Available at http://www.royalmailgroup.com/sites/default/files/Costing_Manual_%202015-1.pdf

- whenever possible, common costs shall be allocated on the basis of direct analysis of the origin of the costs themselves;
- when direct analysis is not possible, common cost categories shall be allocated on the basis of an indirect linkage to another cost category or group of cost categories for which a direct assignment or allocation is possible; the indirect linkage shall be based on comparable cost structures; and
- when neither direct nor indirect measures of cost allocation can be found, the cost category shall be allocated on the basis of a general allocator computed by using the ratio of all expenses directly or indirectly assigned or allocated.

Preliminary view

110 Frontier Economics consider that the 2006 Accounting Direction requirements in relation to cost allocation are consistent with international best practice. Therefore, ComReg's preliminary view is to maintain the current requirements in respect of cost allocation in the Proposed Accounting Direction, pursuant to section 31(3)(a) & (b) of the 2011 Act.

4.2.1.2 Cost drivers

111 Once costs have been classified (as variable, fixed, or avoidable) the USP uses cost drivers to allocate direct and indirect costs to individual services. Where required, general allocator costs are allocated using EPMU[32]. Individual cost drivers use allocations based on volumes, pay, or revenue. For example, the allocation of delivery costs to postal services will depend on the volumes of individual services delivered. The USP's cost drivers typically also use weightings for different mail types as different services use differing amounts of resources.

112 The USP has a total of 139 drivers for allocating costs but only used 72 of them in 2014. The USP applies the drivers in a set sequence, as outlined in Table 3 below. The sequence means that certain drivers rely on costs which have already been assigned. In particular, the general allocator (number 12 in the table below) needs to be allocated once other costs have already been allocated as the formula uses a pro-rata basis based on the ratio of all other costs incurred by the services.

[32] The general allocator formula assigns costs to products on a pro-rata basis by using the ratio of all expenses directly or indirectly assigned to all products.

Table 3. USP's sequence of cost allocation

1.	Volume * Preparation weighting factors, Volume * delivery weighting factors, non-labelled drivers (i.e. volume, turnover), central admin allocation
2.	Central Provision Allocation
3.	Ops Pay
4.	Head-office Pay-Service Volumes
5.	Allocation of terminal dues, delivery, preparation time, publicity post, scale payments delivery
6.	General Allocator Domestic & Inbound, Service Volumes * Transportation Factor Delivery
7.	Volume * collection/transportation/sorting/international Mail/Other weighting factors, Operational Pay drivers (i.e. OP turnover, OP volumes), Non Pay and Operational Pay non-pay cost split,
8.	Direct Ops Pay
9.	Head-office Pay drivers
10.	Total Pay Excluding Scale Payments
11.	Non Pay drivers (i.e. Non Pay volumes, Non Pay turnover), Scale Pay drivers (Scale Pay volumes, Scale Pay turnover), Scale payments, Allocation of Mails by sea and air, Allocation of EMS/foreign Admin Parcels, Inter Service Cost Splits, Delivery Driving Time, Marketing, Election Post
12.	General Allocator All Services

Source: Frontier Economics analysis of the USP's "Driver.csv" file

113 The 2006 Accounting Direction (4.3.4.5) requires the USP's Accounting Manual to provide detail of "*how cost allocation drivers are reviewed, updated and verified*". The cost drivers are a large determining factor in the USP's cost allocation system and it is therefore reasonable that such details be provided.

Preliminary view

114 As Frontier Economics outlines the current level of detail provided by the USP, as to how its cost drivers are set and reviewed, provides very little transparency to ComReg. ComReg agrees and is of the preliminary view that the Proposed Accounting Direction should be strengthened by requiring a greater level of detail as to how cost drivers are set. Pursuant to section 31(3)(b) of the 2011 Act, ComReg proposes that the Proposed Accounting Direction should require the USP:

- to provide in its Accounting Manual the full details of its cost drivers.

- to detail in its Accounting Manual where there has been a year-on-year change in the methodology of its cost drivers, and that the nature and reason of that change is fully detailed by the USP, including the reasons as to why any prior-year adjustment to the Regulatory Accounts has or has not been made.

4.2.1.3 Costs for each universal postal service price

115 Under section 3.2 of the 2006 Accounting Direction, the USP is required to set out a detailed estimate of the costs of providing the service for each price point[33]. At present, the USP's Regulatory Accounts cannot provide this because the USP's costs are split into two weight steps - below and above 50 grams[34] - whereas its tariffs vary across numerous price bands for numerous different weights.

116 The 2011 Act is now in effect and section 28(1)(b) therein requires the USP to ensure that its tariffs for each postal service or part of a postal service are cost-oriented – i.e. that the tariff takes account of and reflects the costs of providing the postal service concerned.

117 In order to comply with section 28(1), the USP has options. The USP must either improve its capability to split its costs by weight step or, in the alternative, it must reduce its number of price bands by weight step for its universal postal services. If the USP was to improve its capability to split costs by weight step, Frontier Economics has considered Royal Mail's service module structure from its ABC Costing Manual and how Royal Mail has more disaggregated costing options so as to align with tariffs. In the alternative, if the USP was to reduce its number of price bands by weight steps for its universal postal services, ComReg notes that the format of the postal packet, that is the size/shape of the postal packet (e.g. letter, large envelope, packet), would facilitate such change given that the format, rather than the weight, of the postal packet is the principal driver of costs.

Preliminary view

118 Having considered the recommendation of Frontier Economics and the requirements of section 28(1) of the 2011 Act, ComReg is of the preliminary view that the updated Accounting Direction should, pursuant to sections 28(1) and 31(3)(b) of the 2011 Act, continue to require the USP:

- to provide the associated cost for each price of a universal postal service;

[33] As required also by Article 12 of the Postal Services Directive: "prices shall be cost-oriented..."
[34] The 50 gram weight break is based on the previous "reserved area", which, up until the 2011 Act, An Post held a monopoly over letters weighing up to 50 grams. This no longer applies as the postal market is now fully liberalised following the implementation of the 2011 Act.

- to provide a detailed explanation in its Accounting Manual of how costs are allocated to services with different tariffs; and

- to provide a detailed explanation in its Accounting Manual of where the weight factors used in the allocation process do not align with the various tariff price points.

4.2.1.4 Inter-company[35] and inter-segments[36] transactions

119 Ensuring that the USP's internal payments and charges are set at an appropriate level is important to ensure accurate cost allocation for the purpose of preparing the Regulatory Accounts. For instance, section 28 of the 2011 Act requires that the USP be able to accurately determine its incurred costs from providing the universal postal service.

120 A well-defined, transparent, and verifiable transfer charging system is therefore necessary in order to demonstrate non-discrimination and to calculate internal costs and revenues. The 2006 Accounting Direction requires that:

- payments/charges between business segments to be calculated on an arm's length basis, and in a transparent and non-discriminatory manner; and

- transfer "charges" shall equal the price the USP would charge any competitor who wished to use its network or pay to any external supplier.

121 While the USP's Regulatory Accounts show the inter-segment revenue by business segment, they do not show the source of that revenue. Such detailed information would provide greater transparency as to the trends and direction of the USP's inter-segment revenue.

Preliminary view

122 ComReg's preliminary view, pursuant to section 31(3)(g) of the 2011 Act, is that the current requirements under the 2006 Accounting Direction, with regard to inter-company and inter-segment charges, should be carried over in the Proposed Accounting Direction. However, given the above and having considered the recommendation of Frontier Economics, ComReg preliminary views is that the Regulatory Accounts should include the source of inter-segment revenue, in a matrix form, in order to show how charges flow between the USP's various operating segments.

[35] Between An Post and its other companies where applicable
[36] Between segments within An Post, for example, between its Mails and Retail divisions

123 Furthermore, given their critical importance, ComReg is of the preliminary view that the nature and detail of all inter-company and inter-segment charges should form part of the scope of the audit conducted by the Regulatory Auditor. This should give ongoing assurance that transfer prices are set at an appropriate level. In particular, the Regulatory Auditor should consider whether transfer charges can be set with reference to market or regulated prices for comparable services. An example of a comparable service for which there is a market rate is the selling of stamps which is done by the USP's Retail division and 3rd parties (postal agents, newsagents, convenience stores etc). Where a comparable open market or regulated price does not exist, transfer prices should be cost-oriented.

4.3 Regulatory Reporting

124 The 2006 Accounting Direction requires the USP to provide ComReg with:

- annual Regulatory Accounts, disaggregated to the level of service; and
- a detailed Accounting Manual outlining the procedures and policies used to prepare the annual Regulatory Accounts, which is to be reviewed annually.

125 In general, Frontier Economics considers the 2006 Accounting Direction requirements in relation to regulatory reporting to be consistent with international best practice. However, there are a number recommendations made by Frontier Economics as to how to further improve the regulatory reporting. ComReg considers that these recommended improvements, if given effect, should reduce the USP's regulatory burden over the medium to long term, by refining and streamlining the reporting process and as a result, reducing the number of ad hoc requests from ComReg for financial information. These proposed improvements are examined below.

4.3.1 Reporting balance sheet at regular intervals

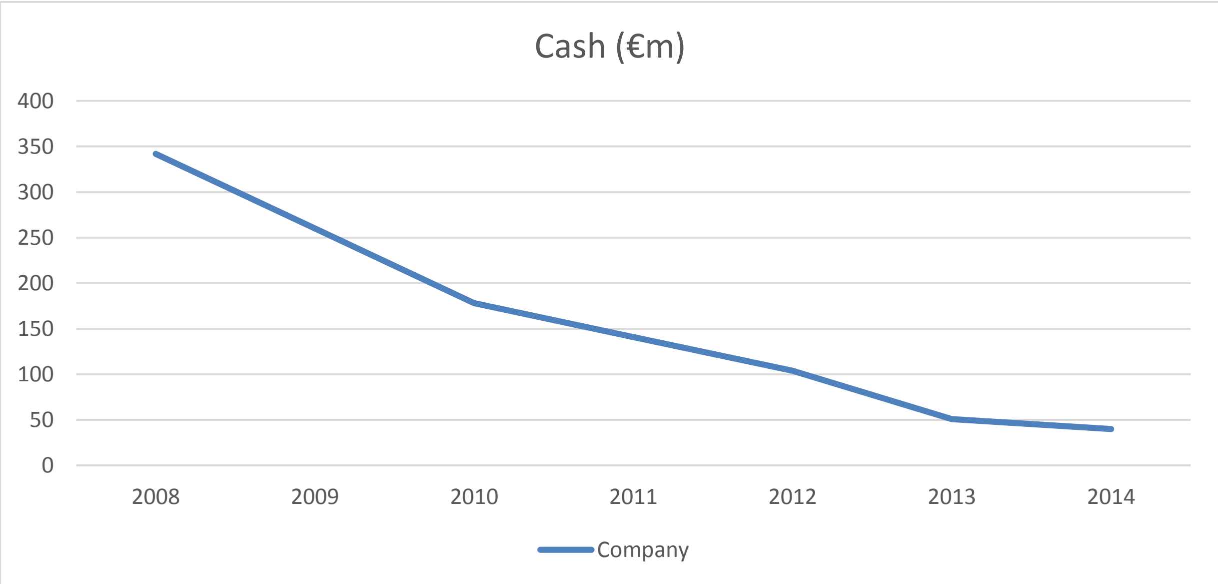
126 The USP currently reports its balance sheet for each business segment, on an annual basis and in accordance with section 3.1(c) of the 2006 Accounting Direction. ComReg uses this this information to assess the USP's ability to meet its universal postal service obligations.

127 ComReg has previously set out its concerns regarding the USP's deteriorating cash position.[37] Given that its overarching remit is to ensure the provision of an affordable universal postal service that meets the reasonable needs of all postal service users, ComReg is concerned that the USP's deteriorating cash position could have a negative impact on the continued provision of the universal postal service. ComReg has a limited statutory remit to regulate the USP's postal services which are not universal postal services and it has no role to regulate the USP in its capacity as a provider of various non-postal products and services. The profitability or otherwise of other parts of the USP's mail and other businesses are for the USP itself to address.

128 ComReg has endeavoured to ensure the continued provision of the universal postal service by setting a 5-year price cap. This should enable the USP to recover its efficient costs and return its universal postal service to a maintained state of profitability. However, returning the universal postal service to profitability is dependent on the USP's actual volume decline being less than or equal to the forecast volume decline (as factored into the price cap decision) and the USP meeting or exceeding its year-on-year efficiency targets (as also factored into the price cap decision).

129 Given the above, ComReg remains concerned about the USP's cash at bank and in hand, as these have continued to decrease[38].

Figure 2. An Post Company cash at bank and in hand (€ million)



Source: ComReg analysis of An Post's audited balance sheets

[37] See ComReg Documents Nos. 14/59, 13/21, 12/138

[38] Furthermore, toward the end of 2014, An Post undertook a sale and finance leaseback arrangement for some of its mails automation equipment. (€16.4 million), therefore if this one off sale process was not undertaken in 2014, and all other things being equal, the An Post Company cash balance would have been c.€28m at the end of 2014 (less than one week's cash).

130 As can be seen from the graph above, the USP's cash at bank and in hand has been worsening year on year, having fallen from c. €350m in 2008 to below €50m by the end of 2014 – on average by c.€50m a year.

131 Under the current 2006 Accounting Direction, any further reduction in the USP's cash balance, as might occur in any given year, would not be known to ComReg until the Regulatory Accounts for that year had been published (usually 4-5 months after the year has ended).

132 Given the USP's current low cash balance at bank and at hand, and the serious concerns this raises, ComReg proposes to require the USP to report the An Post Company balance sheet (which includes its cash at bank and in hand) on a quarterly basis.

133 ComReg would note that the information at issue already exists and is readily available. Therefore, providing this information to ComReg on a quarterly basis should not place an unduly onerous or costly burden on the USP.

Preliminary view

134 ComReg, pursuant to section 31(3)(g) of the 2011 Act, ComReg proposes to include in the Proposed Accounting Direction a requirement that the USP report the An Post Company balance sheet to ComReg on a quarterly basis and within four weeks of the each quarter end. ComReg further proposes that this reporting requirement would cease when or if the An Post Company cash at bank and in hand reaches a sufficient level (€100m) to ensure that provision of the universal postal service is sustainable.

4.3.2 Capital expenditure

135 The USP currently reports its balance sheet for each business segment but it is not required to report, in its annual Regulatory Accounts, on its capital expenditure in respect of its the universal postal service, specifically.

136 As the USP's cash figure has significantly decreased since 2008, there is a concern that the USP could underspend on capital expenditure that is essential for provision of the universal postal service. Under the price cap control, the USP has an allowance for such capital expenditure.

137 The USP does not currently split its capital expenditure between its universal and non-universal postal services. Based on pre-consultation engagement with the USP, it appears that doing so may be practically difficult as it would require the USP to make a number of assumptions, which would be difficult to validate.

138 There could, however, be a benefit in the USP providing additional reporting on its capital expenditure in the Regulatory Accounts, in the form of a more detailed commentary. Having more details of this expenditure would provide increased transparency and should provide greater assurance to ComReg in relation to the sustained provision of the universal postal service.

Preliminary view

139 Given the above and having regard to Frontier's recommendation, ComReg proposes to include in the Proposed Accounting Direction a requirement that the USP, pursuant to section 31(3)(g) of the 2011 Act, shall provide detailed commentary on its capital expenditure in its Regulatory Accounts.

4.3.3 Payroll costs

140 Payroll costs account for a significant proportion of the USP's total expenditure and of the total expenditure required to provide the universal postal service.

141 The USP currently reports some detail of its payroll costs and staff numbers in its Regulatory Accounts.

142 The USP reports its payroll costs at the level of the mails business segment and, within that, the universal postal service and non-universal postal service segments.

143 As noted by Frontier Economics, the reporting of payroll costs could be improved by requiring the USP to report its payroll costs for each business segment and to split its payroll costs between its universal and non-universal postal services. The USP already records this cost split, differentiated by service, as part of its cost accounting system.

144 The USP reports, in its Regulatory Accounts, staff numbers (FTEs) for the company, for combined subsidiaries, and the total at the group level. The USP does not provide further detail of staff numbers. ComReg considers that it would improve information if details of average FTE matched the detail on payroll, that is for each business segment, and split between universal postal service and non-universal postal service. The USP already records this information.

Preliminary view

145 Having considered the recommendation of Frontier Economics, ComReg proposes to include in the Proposed Accounting Direction a requirement that the USP, pursuant to section 31(3)(g) of the 2011 Act, shall provide information on its payroll and average staff numbers (FTE equivalent) by business segment and, for the mails business segment, that it shall split between the universal and non-universal postal services.

4.3.4 Accounts commentary

146 The 2006 Accounting Direction requires the USP to provide commentary in the Regulatory Accounts that, at a minimum, explains:

- trends relating to revenue by relevant postal service;
- trends relating to cost by relevant postal service;
- trends relating to volume by relevant postal service;
- significant period on period movements in the reported performances and balances;
- one-off or exceptional events in the period; and
- the impact of material changes in accounting policies, methodologies and estimation techniques.

147 Frontier Economics' review of the USP's past Regulatory Accounts indicates that the required level of detail, as outlined above, has not always been included in the commentary provided in the Regulatory Accounts. For example, no commentary has been included on trends relating to revenue, cost, and volume by the service level, only at an aggregated level. Given the significant decline in mail volume by service which the USP has experienced, and which may still be ongoing, it is important that sufficient commentary is provided so that ComReg has sufficient information on the availability and future availability of the universal postal service.

Preliminary view

148 ComReg proposes that the existing requirement under the 2006 Accounting Direction in relation to the USP having to provide commentary on the Regulated Accounts, should remain under the Proposed Accounting Direction, pursuant to section 31(3)(g) of the 2011 Act. ComReg is also of the preliminary view that the accessibility of the Regulatory Accounts could be improved by including charts and trends similar to those included in An Post's Annual Report.

4.3.5 Other reporting requirements

149 The USP is currently required to report on its financial performance for its non-universal postal services only at the aggregated level, and not by service as is required for its universal postal services.

150 The non-universal postal service portion of the USP's business has been growing in recent years as a proportion of its total business. If it continues to grow then its impact on An Post's ability to meet its universal postal service obligations could increase.

151 As noted by Frontier Economics, it is important that ComReg, in order to exercise its statutory functions, is able to adequately monitor the USP's non-universal postal services at a service level, when required. This is already facilitated by a requirement under the 2006 Accounting Direction as the USP has to provide any information as may be required by ComReg as an ad hoc report.

152 Furthermore, ComReg may require *ad hoc* reports from the USP in relation to the availability of the universal postal service. For example, ComReg may require information on the cash at bank and in hand forecasts of the USP in order to assess the future availability of the universal postal service.

153 If ComReg should receive any such *ad hoc* report, it may require appropriate verification of some or all of the content of the report. ComReg may therefore require a report from the Regulatory Auditor based on work conducted through "Agreed Upon Procedures"[39] in respect of any such *ad hoc* reports, where required by ComReg from time to time.

Preliminary view

154 ComReg proposes that the existing requirement under the 2006 Accounting Direction, in relation to the USP having to provide, upon request, such an *ad hoc* report as may be required by ComReg, should be carried over in the Proposed Accounting Direction. ComReg also proposes that it may arrange for the Regulatory Auditor to conduct "Agreed Upon Procedures" in respect of for any such *ad hoc* report, as may be requested by ComReg from time to time.

4.3.6 Publication of the Accounting Manual

155 At present, the USP is required to provide its Accounting Manual to ComReg on an annual basis but is not required to publish this document.

156 By comparison, Eircom publishes a version of its equivalent document annually, this being a requirement of the accounting direction to which it is subject.[40] Royal Mail is also required to publish its equivalent document annually, as noted by Frontier Economics.

[39] An "Agreed Upon Procedures" engagement is carried out in accordance with the International Standard on Related Services 4400 'Engagements to perform Agreed Upon Procedures Regarding Financial Information' and does not constitute an examination made in accordance with generally accepted auditing standards. An Agreed Upon Procedures engagement is not an audit.

[40] ComReg D08/10 (http://www.comreg.ie/_fileupload/publications/ComReg1067.pdf). See also Eircom's separated accounts at http://www.eircom.net/regulatoryinformation/separated-accounts/

157 In its pre-consultation engagement with ComReg, the USP raised concerns regarding publishing a version of its Accounting Manual. These relate to concerns that the information contained in the USP's Accounting Manual would be difficult to discern for stakeholders. The USP also raised concerns that much of the information would be confidential and commercially sensitive.

Preliminary view

158 ComReg does not propose to require the USP to publish its Accounting Manual (this maintains the current situation) but ComReg does propose, as a substitute, that the USP shall be required to include in its Regulatory Accounts details of the accounting principles which it applied in preparing its Regulatory Accounts, in sufficient detail as to clearly inform stakeholders as to how those accounting principles were applied.

4.4 Compliance requirements

4.4.1 Regulatory Auditor's verification of compliance with the requirements of the Accounting Direction

159 Section 3.1(j) of the 2006 Accounting Direction requires that a "competent body" (i.e. an auditor) provide a report and opinion on the Regulatory Accounts and the USP's compliance with the requirements of the 2006 Accounting Direction. This includes an audit of the USP's Accounting Manual to ensure that it is consistent with the Accounting Direction.

160 Section 31(3)(d) of the 2011 Act requires that a direction under section 31(1) shall provide for verification by a statutory auditor or statutory audit firm of compliance with internal cost accounting systems. ComReg thus proposes to include, in the Proposed Accounting Direction, details as to the manner in which a statutory auditor or statutory audit firm (that is, the Regulatory Auditor) shall verify compliance by the USP with its internal cost accounting systems. The proposed details are set out below.

Scope of audit

161 Sections 31(3)(a), (b), (c), and (g) of the 2011 Act respectively provide that a direction given by ComReg under section 31(1) shall provide for:

- Rules relating to the identification of costs;
- Rules relating to the allocation of costs;
- Rules relating to the use of internal cost accounting systems for the purposes of identifying and allocating costs (as per (a) and (b)); and
- Such other matters relating to the requirements of section 31 and such a direction as ComReg considers appropriate.

162 The above provisions mean that ComReg must rely heavily on the verification of compliance with internal cost accounting systems, furnished by a statutory auditor or statutory audit firm (that is, the Regulatory Auditor) pursuant to section 31(3)(d) of the 2011 Act.

163 The current scope of the auditor's opinion is provided on a "present fairly" basis.

Preliminary view

164 ComReg, pursuant to section 31(3)(g) of the 2011 Act and having considered the recommendations of Frontier Economics, proposes that the Proposed Accounting Direction should require that the scope of the audit, conducted pursuant to section 31(3)(d) should continue to be on a “present fairly” basis, and that it should include commentary and verification of compliance by the USP with its internal cost accounting systems, in respect of the following:

- the Regulatory Accounts and the Accounting Manual;
- the revenue, costs, and volumes included in the Regulatory Accounts;
- the reconciliation between the Regulatory Accounts and statutory accounts;
- correctness of figures, including operational volumes and the reconciliation of revenue-derived volumes to operational volumes;
- methodologies used regarding amortisation, cost capitalisation, and cost allocation (including transfer charges / inter-segment charges);
- appropriateness of the usage of the cost drivers;
- nature and detail of all transfer charges / inter-segment charges;
- the frequency of updates used for cost allocation purposes;
- appropriateness of any changes in the cost allocation methodology; and
- whether the Accounting Manual continues to fairly present the USP’s processes, procedures, and policies in preparing the Regulatory Accounts.

4.4.2 Appointment of the Regulatory Auditor

165 At present, the auditor of the Regulatory Accounts is contractually appointed by the USP and is the same entity as audits the USP’s statutory accounts.

166 Article 14(5) of the Postal Directive requires that compliance with the cost accounting systems be verified by a competent body which is independent of the USP (emphasis added). Furthermore, a report for the European Commission by WiK (2009[41]) found that where an auditor is appointed and retained by the USP then its independence may be open to question. For this reason, WiK recommended that the NRA in each Member State (ComReg in Ireland) should ensure that the USP's cost accounting practices are verified at least annually, either by the NRA itself or by a competent body appointed by the NRA.

167 Frontier Economics also recommends that the Regulatory Auditor be appointed by ComReg, as this is considered best practice. Frontier Economics further recommends that the auditor of An Post's statutory accounts should not be appointed as the Regulatory Auditor or, if it is appointed, that its regulatory audit should be subject to peer review.

Preliminary view

168 ComReg proposes that the auditor of the Regulatory Accounts (the Regulatory Auditor) should be appointed under contract by ComReg and that the appointed auditor shall not be the same entity as audits An Post's statutory accounts (and as appointed by An Post).

169 ComReg is of the preliminary view that its appointment of the Regulatory Auditor would ensure independence, would be better aligned with best practice and with the requirements of the Postal Directive, and therefore provide greater assurances over the inputs and outputs of the Regulatory Accounts for all parties, including the USP. In particular, given that the Regulatory Auditor would be tasked to review the USP's adherence to the requirements set out in ComReg's accounting direction, it is reasonable and logical that ComReg should appoint this Regulatory Auditor to provide greater assurance to ComReg in relation to adherence by the party subject to the audit (i.e. the USP) with its obligations under the Proposed Accounting Direction. ComReg already appoints and retains the auditor in a related regulatory context in postal where ComReg currently appoints and retains the auditor of the USP's RMS which informs cost allocation (among other things).

[41] 'The Role of Regulators in a More Competitive Postal Market' http://ec.europa.eu/internal_market/post/doc/studies/2009-wik_regulators.pdf

170 ComReg proposes that it will appoint as Regulatory Auditor any statutory audit firm[42] that is currently not a statutory audit firm acting for An Post, following a competitive tendering process, and that the Regulatory Auditor will conduct its audit in accordance with the Proposed Accounting Direction and section 31 of the 2011 Act. The Regulatory Auditor will also have a "duty of care"[43] to the USP (subject to tri-partite arrangement with the Regulatory Auditor). For the avoidance of doubt, ComReg's appointment of the Regulatory Auditor would not impact An Post's separate appointment of an auditor for its statutory accounts prepared pursuant to the Companies Act 2014.

4.4.3 ComReg's approval of the USP's Accounting Manual

171 The 2006 Accounting Direction (section 4.1 (e)) requires the USP to obtain ComReg's approval for each annual edition of the Accounting Manual in advance of the start of the relevant regulatory period. In practice, this has not been done.

Preliminary view

172 ComReg proposes that it would be more efficient if the USP was only required to notify ComReg of any changes to the Accounting Manual and if it was not required to obtain ComReg's approval for each annual edition of the Accounting Manual. To ensure that the Accounting Manual correctly sets out the procedures and policies for preparing the Regulatory Accounts, ComReg proposes that the Regulatory Auditor would assess any such changes and would report to ComReg as to whether the Accounting Manual continues to fairly present the USP's processes, procedures, and policies in preparing the Regulatory Accounts.

4.4.4 Statement of compliance

173 The 2006 Accounting Direction (section 3.1 (i)) requires a signed statement from the Directors of An Post acknowledging their responsibilities for the preparation of the Regulatory Accounts and confirming their compliance with the requirements of the 2006 Accounting Direction. This requirement is similar in scope to that of Eircom, under the separate accounting direction to which it is subject.

174 Section 31(3)(f) of the 2011 Act requires the publication of a statement relating to compliance with section 31 of the 2011 Act and with any direction given under section 31 of the 2011 Act. As the Regulatory Accounts and Accounting Manual will be prepared to meet obligations under section 31, the signed statement of compliance will acknowledge the Directors of An Post responsibility in preparation of same.

[42] Having the meaning assigned to it under the European Communities (Statutory Audit) (Directive 2006/43/EC) Regulations 2010 (S.I. No 220 of 2010)

[43] To mirror the existing "duty of care" given to ComReg by the auditor where An Post appoints and retains the auditor – see Information Notice 12/19 dated 12 March 2012

Preliminary view

175 ComReg proposes that the Proposed Accounting Direction shall maintain the requirement that the Directors of An Post furnish a signed statement, acknowledging their responsibilities for the preparation of the Accounting Manual and the Regulatory Accounts and confirming that said documents comply with section 31 of the 2011 Act and with the Proposed Accounting Direction.

4.5 Timetable to comply with Direction

176 ComReg is of the preliminary view that the USP should be able to implement the proposals for the Proposed Accounting Direction within a reasonable timeframe as:

- many of the proposed requirements exist under the 2006 Accounting Direction, and
- where any proposed information requirements are additional to the existing information requirements under the 2006 Accounting Direction, the USP already has much of the information at issue in its possession.

177 ComReg is thus of the preliminary view that the USP should be in full compliance with the requirements of the Proposed Accounting Direction, given under section 31 of the 2011 Act, by the start of financial reporting period commencing 1 January 2017, in order that the Regulatory Accounts ending 31 December 2017 shall be fully compliant with the Proposed Accounting Direction (when made).

4.6 Conclusion on updating the Accounting Direction

178 ComReg has, above, set out above its preliminary views on the Proposed Accounting Direction which would issue under section 31 of the 2011 Act, as follows:

(1) Measuring mail volumes and revenues

(2) Cost identification and allocation

(3) Regulatory reporting

(4) Compliance requirements

(5) Timetable to comply with Direction

(6) Format of Regulatory Accounts.

Q. 1 Do you agree or disagree with ComReg's preliminary views on updating the Accounting Direction? Please explain your response and provide any supporting evidence.

4.7 Format of the Regulatory Accounts

179 Given the preliminary views on updating the Accounting Direction, Frontier Economics has developed a draft version of the proposed Regulatory Accounts format pursuant to the Proposed Accounting Direction (to be made) and section 31 of the 2011 Act. ComReg agrees with the proposed Regulatory Accounts format as set out in Document No. 15/135b, which reflects the preliminary views made by ComReg in this consultation. For the most part, the draft version of the proposed Regulatory Accounts format reflect the existing format of the Regulatory Accounts prepared in accordance with the 2006 Accounting Direction (Document No. 06/63); so that this is clear, for the proposed format of the Regulatory Accounts as set out in Document No. 15/135b, any additional information requirements have been highlighted in yellow.

180 The USP, in its pre-consultation engagement with ComReg, has submitted what it considers appropriate for the format of the Regulatory Accounts. Details of the material submitted by the USP are in Document Nos. 15/135d and 15/135e, published alongside this consultation paper. The “Long Form” therein (Document No. 15/135d) is the proposed version of the Regulatory Accounts that would be submitted in confidence to ComReg while the “Short Form” (Document No. 15/135e) is the non-confidential version of the Regulatory Accounts that would be published by the USP and would contain significantly less information than the “Long Form”. ComReg has considered the USP's submitted proposals but is of the preliminary view that they do not accord with ComReg's preliminary views, as set out in this consultation paper, and that they do not meet the requirements set out in section 31 of the 2011 Act nor do they meet certain other key requirements of the 2011 Act (for example, the requirements under sections 28 & 29).

181 The proposed format of the Regulatory Accounts schedule as set out in Document No. 15/135b has been developed in order to minimise ambiguity with regard to Accounts' content, format and level of detail required. The Regulatory Accounts schedule includes required areas of commentary to help ensure sufficient commentary is provided. The schedule includes detailed commentary in the “regulatory accounting principles and basis of preparation” section on large adjustments made to produce the Regulatory Accounts, the impact of changes in accounting policies, methodologies and estimation techniques, and transfer charges (including a detailed explanation regarding the basis of transfer charges).

182 The proposed format also improves the accessibility of the Regulatory Accounts by including additional information such as per unit revenue, cost and profit/loss details for each universal postal service. While this information is already provided in the Regulatory Accounts in aggregate form, including this information on a per unit basis improves transparency and results in the Regulatory Accounts being more user friendly.

183 It is ComReg's preliminary view that the service level should include parcels as a separate category, as the current Regulatory Accounts do not provide disaggregated information on parcels. Given the growth in e-commerce, parcels are potentially a large component of revenues, and therefore it would seem to be appropriate for it to be a separate line item, rather than including it in "other" as is the case currently. This would also ensure that the reporting of parcels is consistent with the reporting of packets (smaller parcels).

4.6.1 Confidential and public versions of Regulatory Accounts

184 The USP prepares its Regulatory Accounts and submits these to ComReg. The USP also publishes its Summary Regulatory Accounts[44], an extract of the Regulatory Accounts redacting certain information which the USP considers to be confidential / commercially sensitive. This redacted information is:

- detail on the split of costs by Revenue Collection, Collection, Outward Sorting, Transport, Inward Sorting;
- detail on the reconciliation of revenue-derived and operational based volumes by format.

185 Therefore, as can been seen above, the Summary Regulatory Accounts that the USP currently publishes does not have many redactions and is much the same as the Regulatory Accounts submitted in confidence to ComReg.

186 As is the current case, in ComReg's proposals for this public consultation, there are the Regulatory Accounts to be submitted to ComReg (proposed template at Document No. 15/135b) and a Summary Regulatory Accounts (proposed template at Document No. 15/135c) which is the public version of the Regulatory Accounts with redactions for information that is deemed to be confidential/commercially sensitive and therefore, as such, cannot be published.

[44] http://www.anpost.ie/NR/rdonlyres/354DFCDE-E9F4-49C4-9435-E8F337222F2C/9086/ANPOST_SummaryRegulatoryAccounts2014.pdf

187 ComReg proposes that the existing publication by An Post of Summary Regulatory Accounts should continue and the proposed Summary Regulatory Accounts at Document No. 15/135c reflect this. Therefore, for the additional information requirements proposed for this updated Accounting Direction, ComReg needs to assess whether they should be made public or not. Data is more likely to be commercially sensitive only where the USP faces competition or prospective competition. Universal postal services do not face competition or likely prospective competition.

Preliminary view

188 Having considered the recommendation of Frontier Economics, ComReg's preliminary view in relation to the confidentiality of the additional information requirements proposed for the updated Accounting Direction are as follows:

Additional information	Proposed treatment
Commentary and additional KPI in "1 Financial Summary and Business Review"	Public as does not contain confidential information
Commentary on USO volumes in "3 USO Performance"	Public as does not contain confidential information
Split on International Inbound profit/(loss) between intra-Community and Rest of World	Public as does not contain confidential information; improves information for section 29 of 2011 Act
Split on intra-segment revenue and cost, USO and non-USO	Public as does not contain confidential information
Per unit Revenue, Cost and Profit(Loss) for each universal postal service	Public as does not contain confidential information; improves information for section 28(1) of 2011 Act
Split non-USO Parcels from other	Confidential as relates to non-USO Parcels
International Inbound by intra-Community and Rest of World	Public as does not contain confidential information
Estimated cost of providing universal postal service by price point	Confidential
Average FTE and Payroll costs by business segment, USO, non-USO	Public as does not contain confidential information

Additional information	Proposed treatment
Reconciliation of operational volumes at format level by Mail Centre and DSU	Public as does not contain confidential information
Quarterly balance sheet, if cash at bank and in hand is less than €100m	Confidential for quarterly submission to ComReg within four weeks of quarter end. Annual balance sheet and quarterly balance sheets that pre-date the Annual balance sheet published in Regulatory Accounts as the quarterly balance sheet would no longer be confidential as annual balance sheet published by An Post in its Annual Report.

189 The proposals above are reflected in the proposed Regulatory Accounts at Document No. 15/135b and the proposed Summary Regulatory Accounts at Document No. 15/135c.

Q. 2 Do you agree or disagree with ComReg's preliminary views on the format of the Regulatory Accounts as set out in ComReg 15/135b? Do you agree or disagree with ComReg's preliminary views on what in the Regulatory Accounts is made public as set out above and in the Summary Regulatory Accounts set out in ComReg 15/135c? Please explain your response and provide any supporting evidence.

5 Draft Regulatory Impact Assessment

190 The Regulatory Impact Assessment Guidelines [45] (Document No. 07/56a), made in accordance with a Ministerial Policy Direction[46], state that the Commission for Communications Regulation ("ComReg") will conduct a Regulatory Impact Assessment ("RIA") in any process that may result in the imposition of a regulatory obligation, or the amendment of an existing obligation to a significant degree, or which may otherwise significantly impact on any relevant market or any stakeholders or consumers.

191 This consultation concerns a proposal by ComReg to give a direction to An Post, the sole universal postal service provider ("USP"), pursuant to section 31(1) of the Communications Regulation (Postal Services) Act 2011 ("2011 Act"). The "Proposed Accounting Direction" would provide for the keeping by the USP, in its internal accounting system, of separate accounts for each service it provides – (a) which is part of the universal postal service, and (b) which is not part of the universal postal service. ComReg proposes to give the direction on the basis that the condition in section 31(2)(c) of the 2011 Act is met – i.e. that ComReg is satisfied that competition in the market for postal services is not fully effective[47]. In addition, section 31(3) provides that a direction give under section 31(1) *shall* provide for -

(a) rules relating to the identification of costs,

(b) rules relating to the allocation of costs,

(c) rules relating to the use of internal cost accounting systems for the purposes of the matters referred to in paragraphs (a) and (b),

(d) the verification by a statutory auditor or statutory audit firm of compliance with internal cost accounting systems,

(e) the publication of such accounts and other information relating to requirements under this section and such direction, as the Commission considers appropriate,

[45] Which have regard to the RIA Guidelines issued by the Department of An Taoiseach in June 2009
[46] Ministerial Policy Direction made by Dermot Ahern T.D. Minister for Communications, Marine and Natural Resources on 21 February, 2003
[47] Condition 31(2)(c) is in effect as ComReg is satisfied that competition in the market for postal services is not fully effective. ComReg made this opinion in Decision D13/13, dated 6 September 2013, in order to make the price cap decision that applies for 5 years (subject to potential review at 3 years), and ComReg is also of the view that this situation is unchanged as at the present date:
"*The Commission for Communications Regulation, pursuant to section 30(2) of the Communications Regulation (Postal Services) Act 2011 ("2011 Act"), is of the opinion that the universal postal services specified in the Communications Regulation (Universal Postal Service) Regulations, 2012 (S.I. 280 of 2012) constitute a separate market and that there is no effective competition in that market*…"
If this situation were to change, that is, if ComReg found that certain universal postal services do face effective competition, then this would require ComReg to revise its specification of the universal postal service so that such postal services are no longer universal postal services as they face effective competition.

subject to the protection of any information which the Commission considers confidential (within the meaning of section 24 of the Principal Act),

(f) the publication of a statement relating to compliance with this section and such direction, and

(g) such other matters relating to the requirements of this section and such direction, as the Commission considers appropriate.

192 It is apparent, from the above provisions, that ComReg has discretion as to whether to give a direction under section 31(1) of the 2011 Act but that if ComReg should decide that giving such a direction is required then, under section 31(3), the direction must provide for the various issues contained in paragraph (a)-(g) therein, as listed above.

193 ComReg would note that most of the obligations contained in the Proposed Accounting Direction are already existing obligations under the 2006 Accounting Direction, which is currently in effect. Therefore, if the Proposed Accounting Direction was put into effect then these various obligations would not be new obligations, in terms of their purpose and effect, but would merely be existing obligations that were being carried over into a new direction issued under current statutory provisions. ComReg considers it unnecessary to conduct a RIA in respect of such obligations which already exist and are being carried over. A RIA is only being conducted in respect of those obligations which, if brought into effect under the Proposed Accounting Direction, would constitute new obligations. This draft RIA will thus assess the proposed obligations of the Proposed Accounting Direction which are additional to those contained in the 2006 Accounting Direction. ComReg invites interested parties to submit their views in respect of this draft RIA. Subject to respondents' views and consideration of any other evidence, this draft RIA will be set out in its finalised form in ComReg's response to consultation.

5.1 Steps involved

194 ComReg's RIA follows five steps:

Step 1: describe the policy issue and identify the objectives

Step 2: identify and describe the regulatory options

Step 3: determine the impacts on stakeholders

Step 4: determine the impacts on competition

Step 5: assess the impacts and choose the best option

Step 1: Describe the policy issue and identify the objectives

195 The USP is currently subject to the 2006 Accounting Direction[48].

196 In Decision D13/13[49], ComReg formed the opinion that competition in the market for postal services is not fully effective in order to make a price cap decision that applies for five years. That remains ComReg's opinion and ComReg is thus satisfied that the condition in section 31(2)(c) of the 2011 Act is met such that ComReg may give a direction to the USP under section 31(1) of the 2011 Act. Such a direction provides for the keeping by the USP, in its internal accounting systems, of separate accounts for each service it provides – (a) which is part of the universal postal service, and (b) which is not part of the universal postal service. In addition, section 31(3) provides that such a direction shall provide for the various issues contained in paragraph (a)-(g) therein, as are listed in paragraph 191 above. The policy is thus to give effect to the provisions in section 31 of the 2011 Act and the key objective is to give a direction to the USP which shall provide for the various issues contained in sections 31(3)(a)-(g) of the 2011 Act.

Step 2: Identify and describe the regulatory options

197 As noted above, the Proposed Accounting Direction, as currently drafted, for the most part provides for a continuation of the 2006 Accounting Direction. However, as set out in this consultation paper, it is ComReg's preliminary view that the 2011 Act imposes various duties on ComReg and the USP which necessitate that certain additional requirements be set out in any direction given under section 31(1). ComReg thus considers that it has two main options:

Option 1 – maintain the status quo by giving a direction to the USP under section 31(1) of the 2011 Act which would maintain the same set of requirements as are currently contained in the 2006 Accounting Direction.

Option 2 – alter the status quo by giving a direction to the USP under section 31(1) of the 2011 Act which would maintain the same set of requirements as are currently contained in the 2006 Accounting Direction, while also imposing certain new requirements (which are set out, below, as individual sub-options within Option 2).

Option 1: Maintain the status quo

198 Option 1 would result in the current requirements contained in the 2006 Accounting Direction being maintained. The only real change would be that the requirements would no longer be given effect under the old statutory framework but would be brought into effect under the current statutory framework, in place since August 2011.

[48] ComReg Document No. 06/63
[49] ComReg Document No. 13/82

Option 2: Include the additional requirements as set out in the Proposed Accounting Direction

199 Option 2 would result in an updated Accounting Direction that maintained the requirements contained in the 2006 Accounting Direction but added some further information requirements[50], in order that ComReg and the USP can discharge their respective obligations and duties under the 2011 Act. The proposed additional information requirements are as follows:

- Option 2a: Require the USP to provide greater commentary on the existing reconciliation between its revenue-derived mail volumes and its operational-based mail volumes, at the format[51] level.

- Option 2b: Require the USP to reconcile, by format, between its operational mail volumes recorded at the DSU and Mail Centre level.

- Option 2c: Require that the USP's revenue derived and operational based mail volume reconciliations be audited by the Regulatory Auditor.

- Option 2d: Require the USP to review its average container fill assumptions quarterly rather than annually.

- Option 2e: Require the USP's Accounting Manual to provide detailed information on the process of identifying avoidable, variable, and fixed costs, including worked examples.

- Option 2f: Require the USP's Accounting Manual to:

    - provide full details of the USP's annual review of its cost drivers.

    - detail where there has been a year-on-year change in the methodology of cost driver(s), and that the nature and reason of that change is fully detailed by the USP.

- Option 2g: Require the USP to include in the Regulatory Accounts the source of inter-segment revenue, in a matrix form, in order to show how charges flow between various USP operating segments.

- Option 2h: Require that the nature and detail of all inter-segment changes be audited by the Regulatory Auditor.

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[50] Each additional requirement is examined as a separate option under Option 2 in this draft RIA.
[51] By letter, large envelope, packet, parcel

- Option 2i: Require the USP to report its balance sheet (including cash at bank and in hand) to ComReg on a quarterly basis.
- Option 2j: Require the USP to include detailed commentary on its capital expenditure.
- Option 2k: Require the USP to report on its payroll costs and average staff numbers (FTE equivalent) for each business segment, and to split between universal postal service and non-universal postal service.
- Option 2l: Require that the auditor of the Regulatory Accounts (the Regulatory Auditor) be appointed by ComReg.
- Option 2m: Specify that the USP shall only be required to notify ComReg of any changes to the Accounting Manual and shall no longer be required to seek approval from ComReg for those changes.

Steps 3, 4 and 5: Determine and assess the impacts on stakeholders and competition and choose the best option

200 Option 1 would result in no additional significant impact on the USP. However, ComReg is of the preliminary view that Option 1 would not meet the information requirements of ComReg pursuant to section 31 of the 2011 Act, so that it could fulfil its statutory functions and objectives, and that it would result in ComReg and the USP not being able to fully discharge their respective obligations and duties under the 2011 Act.

201 Each sub-option under Option 2 is assessed individually below and ComReg has also considered the overall impact of these various sub-options under Option 2 as against maintaining the status quo under Option 1.

- Option 2a: The USP already provides a reconciliation at format level in the confidential version of its Regulatory Accounts provided to ComReg. The proposal here is to require the USP to provide more detailed commentary in relation to the existing reconciliation.
- Option 2b: This proposed requirement should provide ComReg with added assurance as to the accuracy of USP's mail volume counts. This is particularly important given the price cap control in place until 2019, and the risk of any future volume declines which exceed the declines forecast by the USP, which were factored into the price cap control. This option should not be onerous on the USP and is a matter of more detailed reporting.

- Option 2c: If the USP's volume reconciliation was audited by the Regulatory Auditor then this would provide ComReg and the USP with greater confidence as to the accuracy of the USP's mail volume measurements, over time. This is particularly important because there is, at present, relatively little information in the Regulatory Accounts explaining the divergence between the revenue derived and operational based mail volume figures. This proposal would increase the cost of the regulatory audit but the foreseen benefits, in terms of greater assurance and confidence in relation to the USP's volume measurements, should outweigh these additional costs, particularly given the importance of mail volumes to the sustainability of the universal postal service.

- Option 2d: This should improve the accuracy of non-machine counts with minimal additional cost to the USP. Given that non-machine counts account for a very small proportion of operational volumes this should not be an unduly onerous requirement for the USP. The benefit would be having greater confidence in relation to the accuracy of the USP's non-machine counts, particularly for packets and parcels.

- Option 2e: ComReg considers that the issue of identifying avoidable costs is particularly important as ComReg may require details of how the USP identifies its avoidable costs in order to carry out its statutory functions. For example, section 31 of the 2011 Act requires ComReg, in certain circumstances, to resolve disputes, should they arise, between USP and those seeking access to its network. Calculating access prices may involve ComReg having to consider the USP's avoidable costs - for example, the costs that USP would avoid if it granted another postal provider access to its network. Further, any evaluation of the net cost of the USO would require estimating those costs that would be avoided if the USP was not subject to the USO. There may be additional costs to the USP in developing reporting processes to identify fixed, variable, avoidable costs, but such costs are necessary in order for the USP to comply with its various statutory and regulatory obligations.t

- Option 2f: This should improve transparency in relation to how the cost drivers are set and reviewed and should create no or minimal additional costs to the USP, as the proposed requirement relates to the USP giving more detailed reporting on tasks that it already carries out.

- Option 2g: This should provide greater transparency as to the trends and direction of the USP's inter-segment revenue and should create no or minimal additional costs for the USP as the proposed requirement relates to the USP giving more detailed reporting on information that is already available to it.

- Option 2h: This should provide for greater ongoing assurance that transfer prices are set at an appropriate level which is important for ensuring accurate cost allocation. This proposal would likely add to the cost of the regulatory audit but the likely benefits of having greater assurance and confidence in relation to the USP's transfer charges should outweigh this additional cost, particularly given certain obligations placed on the USP, such as, for example, having to ensure that there is no cross subsidisation.

- Option 2i: Given the significant decline in An Post Company cash position, this option should increase transparency in relation to An Post Company cash position and financial position and ensure that ComReg is kept more up to date on An Post’s cash position, as this concerns the current and future sustainability of the universal postal service provision. Further, there should be no additional cost to the USP in providing this information as the information is already produced by the USP on a monthly basis.

- Option 2j: Details of the USP’s capital expenditure should increase transparency and provide greater assurance to ComReg in relation to the USP’s performance, especially if there is a concern that the USP could under spend on necessary capital expenditure for the universal postal service. There should be minimal additional cost to the USP in providing this information, as it is just a matter of more detailed reporting.

- Option 2k: This should increase transparency in relation to this cost which accounts for a significant proportion of total expenditure. The USP already records this required information and therefore there would be no additional cost in providing such information.

- Option 2l: This proposed requirement should represent a better alignment with best practice, should meet the requirements of the Postal Directive, and should provide greater assurance on the inputs and outputs of the Regulatory Accounts. The cost of the regulatory audit will likely increase the cost of regulation which in turn may increase the amount required to be recovered by the postal levy; however, it should also reduce the cost to the USP as the USP would not be paying for the independent auditing of the Regulatory Accounts.

- Option 2m: This recognises that the Accounting Manual is for the USP to prepare and maintain. The Regulatory Auditor will assess whether the Accounting Manual fairly presents the USP’s processes in preparing the Regulatory Accounts and will report to ComReg on this.

202 For the reasons set out above, ComReg considers that Option 2 is the best option and that all of the sub-options within Option 2 should be taken. Option 2 is proportionate and should ensure that the Accounting Direction meets ComReg's requirements pursuant to section 31 of the 2011 Act and that both ComReg and the USP can discharge its respective obligations under the 2011 Act and ComReg Decisions/Regulations. Furthermore, ComReg considers that most of the sub-options under Option 2 could be implemented with no or minimal additional cost to the USP as it would appear that the various items of additional information that would be required is already being produced by the USP. Where an option under Option 2 would likely result in an additional cost, ComReg is of the preliminary view that the resultant benefits should outweigh that additional cost.

Q. 3 Do you have any views on this draft Regulatory Impact Assessment and are there other factors ComReg should consider in completing its Regulatory Impact Assessment? Please explain your response and provide details of any factors that should be considered by ComReg.

6 Draft Accounting Direction

203 The draft Accounting Direction below is based on the existing 2006 Accounting Direction but with certain amendments made, as required, in order to take account of any revisions or additional requirements as proposed in this consultation and also to revise and update the text, as necessary, to reflect that this draft Accounting Direction is made pursuant to the 2011 Act.

Direction on the accounting obligations of the universal postal service provider

1. **STATUTORY FUNCTIONS AND POWERS**

1.1 This Direction (hereinafter referred to as “the **Direction**”) is hereby made by the Commission for Communications Regulation (“ComReg”) for the purpose of directing the universal postal service provider to provide separate accounts in its internal accounting system for each service it provides which is (a) part of the universal postal service, and (b) which is not part of the universal postal service, pursuant to section 31 of the Communications Regulation (Postal Services) Act 2011 and is made:

i. Having regard to ComReg’s functions and objectives set out in sections 10 and 12 of the Communications Regulation Act of 2002 (as amended);

ii. Having taken account of the representations of interested parties submitted in response to ComReg Document No. 15/135; and

iii. Having regard to the analysis and reasoning set out in ComReg Document No. [XX/XX] (Decision [XX/XX]); which shall, where appropriate, be construed together with this Direction.

2. **DEFINITIONS**

2.1 In this Direction, unless the context otherwise suggests, the following terms shall have the following meanings:

“2011 Act” means the Communications Regulation (Postal Services) Act 2011;

“Accounting Manual” has the meaning as per section 5 of this Direction;

"Agreed Upon Procedures" means an engagement carried out by the Regulatory Auditor in accordance with the International Standard on Related Services 4400 'Engagements to perform Agreed Upon Procedures Regarding Financial Information' (as may be amended from time to time) and does not constitute an examination made in accordance with generally accepted auditing standards;

"An Post Company" has the meaning as per An Post's Statutory Accounts;

"Average Container Fill" means conducting a manual count of postal packets by counting the number of containers containing non-machinable postal packets and multiplying that number by the average number of postal packets per container;

"Cash at bank and in hand" has the meaning as per An Post's Statutory Accounts;

"ComReg" means the Commission for Communications Regulation;

"Format" means by letter, large envelope, packet, parcel as defined by S.I. 280 of 2012;

"GAAP" means "Generally Accepted Accounting Principles" as applied in Ireland, unless otherwise specified;

"IFRS 8" means International Financial Reporting Standard 8 "Operating Segments" issued by the International Accounting Standards Board;

"Inter-company transaction" means transactions between the An Post Company and other companies within the An Post Group;

"Inter-segment transactions" means transactions within the An Post Company, for example, between its Mails and Retail divisions;

"Postal Directive" means Directive 97/67/EC of the European Parliament and of the Council, as amended;

"Obligations on Universal Postal Service Providers" means the obligations and principles to be observed by Universal Postal Service Providers under the 2011 Act and/or under any decision, determination or regulations made by, or direction given by, ComReg under the 2011 Act;

“Regulatory Accounts” means the separate accounts kept by the USP in its internal accounting system for each service it provides which is (a) part of the universal postal service, and (b) not part of the universal postal service, in the format prescribed in ComReg Document No. [XX/XXb] and meeting the requirements set by this Direction;

“Regulatory Auditor” means a statutory auditor or firm of statutory auditors appointed by ComReg to review the Regulatory Accounts and Accounting Manual in accordance with this Direction and with International Standards on Auditing (UK and Ireland);

“Service” means a “postal service” as defined by the 2011 Act;

“S.I. 280 of 2012” means the Communications Regulation (Universal Postal Service) Regulations 2012;

“Statutory Accounts” means the statutory accounts prepared by the USP in accordance with sections 32 and 33 of the Postal and Telecommunications Services Act 1983 and Article 15 of the Postal Directive;

“Summary Regulatory Accounts” means Regulatory Accounts published on An Post’s website redacted for confidential and commercially sensitive information and set out in the format prescribed in ComReg Document No. [XX/XXc] and meeting the requirements set by this Direction;

“Tariff Requirements” means the requirements set out in section 28 of the 2011 Act;

“Terminal Dues Requirements” means the requirements set out in section 29 of the 2011 Act;

“Transfer Charge” means charges for Inter-company transactions / Inter-segment transactions;

“Universal Postal Service” means the postal services set out in section 16 of the 2011 Act and SI 280 of 2012 and any future regulations, which may replace S.I. 280 of 2012, made pursuant to section 16(9) of the 2011 Act;

“Universal Postal Service Provider” means the “USP” or any other legal person designated by section 18 of the 2011 Act. An Post is the designated USP pursuant to section 17 of the 2011 Act.

All other terms used in this Direction have the same meaning as per the defined terms set out in section 6 of the 2011 Act.

3. FUNDAMENTAL REQUIREMENTS

3.1 The USP is required by this Direction to keep, in its internal accounting systems, separate accounts for each service it provides which is (a) part of the universal postal service, and (b) not part of the universal postal service and the USP is further required to ensure that said accounts meet the requirements set out below, which requirements are established under this Direction pursuant to section 31(3) of the 2011 Act. These separate accounts are together defined and referred to herein as the "Regulatory Accounts".

3.2 The Regulatory Accounts shall contain sufficient detailed information so as to ensure that ComReg and/or the USP can use that information:

a) to assess whether the USP is complying requirements under the 2011 Act, in particular with the Tariff Requirements under section 28 of the 2011 Act and the Terminal Dues Requirements under section 29 of the 2011 Act; and

b) to respond in a prompt manner to any request for information made by the European Commission pursuant to sections 31(4) and 31(5) of the 2011 Act.

4. REPORTING AND TRANSPARENCY

4.1 Regulatory Accounts

4.1.1 The Regulatory Accounts shall contain the information specified in the following paragraphs (a) – (m) incl.:

(a) The Regulatory Accounts shall contain a commentary on the USP's financial performance that shall identify and explain:

- trends relating to postal services and expected significant future events and how these might impact on the USP's businesses;
- trends relating to revenue, by service;

- trends relating to the mail volumes, by service;
- significant year-on-year movements in the reported performance and balances, in particular the cash at bank and in hand balance;
- one-off or exceptional events in the year;
- large adjustments made to produce the Regulatory Accounts; and
- the impact of changes in accounting policies, methodologies and estimation techniques including the detail of any prior-year adjustments.

(b) The Regulatory Accounts shall contain a comprehensive explanation of the basis of preparation of the Regulatory Accounts, including an explanation of the key accounting policies adopted and applied by the USP. This shall include details of the USP's income recognition policy, depreciation policy, and capitalisation policy, and details of the USP's approaches to dealing with issues such as cost identification, cost allocation, prior year adjustments and changes in accounting policy.

(c) The Regulatory Accounts shall contain profit and loss accounts and balance sheets for each operating segment, as defined in IFRS 8 and as agreed by ComReg, and as prepared in accordance with IFRS 8. These profit and loss accounts and balance sheets shall show data for the USP's last complete financial year and for the financial year immediately prior to that and where the figures are not comparable (because, for example, of some change in accounting policy or other some other reason (as may be applicable)), the figures for the preceding financial year shall be adjusted with full details provided on this prior-year adjustment.

(d) The Regulatory Accounts shall be fully reconciled to the Statutory Accounts, identifying in detail all adjustments required to reconcile between the Regulatory Accounts and the Statutory Accounts.

(e) The Regulatory Accounts shall be presented in the formats and to level of detail shown in the schedules as determined by ComReg and as set out in ComReg Document No. [XX/XX]b and for the Summary Regulatory Accounts as set out in ComReg Document No. [XX/XX]c.

(f) The Regulatory Accounts shall contain detailed commentary and information on capital expenditure by the USP in the provision of the universal postal service.

(g) The Regulatory Accounts shall detail the balance sheet for each quarter of the financial year for the An Post Company.

(h) The Regulatory Accounts shall contain payroll costs and average staff numbers (average FTE equivalent) for each business segment, and for the Mails business segment split between universal postal service and non-universal postal service.

(i) The Regulatory Accounts shall contain volume information that shows mail volume, by service, recorded from revenue data recorded at the point of sale. A supplementary schedule shall also be provided which:

- reconciles, by format, revenue derived volumes with operational data recorded in the outward phase of the postal pipeline, together with the details of volume trends by format recorded using the two methods;
- reconciles quarterly mail volumes, by format, as between operational volumes recorded at the Delivery Service Unit and Mail Centre level.

(j) The Regulatory Accounts shall set out the revenue attributed to each service while distinguishing between (i) revenues which have been directly allocated to specific services, and (ii) revenues which have been allocated or apportioned on the basis of statistical sampling or other accounting allocator.

(k) The Regulatory Accounts shall contain details of expenditure by pipeline process, distinguishing between:

- costs directly allocated to specific services,
- costs indirectly allocated to specific services,
- common costs allocated on the basis of the origin of the costs themselves, and
- common costs allocated on the basis of a general allocator.

(l) The Regulatory Accounts shall contain a written and signed statement from the Directors of An Post Company in which they acknowledge their responsibilities with regard to the preparation of the Regulatory Accounts and the Accounting Manual and confirm that they and An Post Company have, in their opinion, complied with the 2011 Act, and in particular with section 31 thereof, that that they have complied with the requirements set down under this Direction.

(m) The Regulatory Accounts shall contain the results of the annual review of any statistical sampling process undertaken to identify revenue or mail volumes.

The USP shall prepare the Regulatory Accounts in accordance with the following principles:

4.1.2 Inter-company/inter-segment transactions

4.1.2.1 Revenues and costs shall initially be directly assigned by the USP to its operating segments in accordance with the principles set out in IFRS 8. Fixed assets (buildings, vehicles, sorting equipment, etc.) shall be shown in the balance sheet of the “prime user”, with use by other operating segments charged for on an arm’s length basis.

4.1.2.2 Inter-company transactions and Inter-segment transactions shall be calculated on an arm’s length basis and in a transparent and non-discriminatory manner, with the proviso that this Transfer Charge shall equal the price USP would or does charge to any third party user for a similar transaction.

4.1.2.3 The Regulatory Accounts shall clearly identify the source of each inter-company / inter-segment revenue and shall set the sources out in a matrix form, in order to show how charges flow between the USP’s various operating segments.

4.1.3 Mail Volume and Revenue Identification

4.1.3.1 Within the operating segments as defined by IFRS 8, mail volumes and revenue shall be allocated to each service in the following manner:

(a) Mail volumes and revenues which can be directly assigned to particular services shall be so assigned.

(b) Mail volumes, by service, shall be recorded separately, from (i) revenue data recorded at the point of sale; and (ii) operational data recorded in the outward phase of the postal pipeline.

(c) Revenue, by service, shall be recorded at the point of sale.

(d) Any mail volumes and revenues recorded at the point of sale which cannot be directly assigned to specific services shall be apportioned to services on the basis of statistical sampling accurate to +/-1% at the 95% Confidence Level.

(e) The Regulatory Accounts shall apportion any operational-based mail volumes recorded in the outward phase of the postal pipeline, which cannot be directly assigned to their specific services (e.g. manually sorted postal packets), on the basis of statistical sampling, by service, with a minimum margin of error as agreed with ComReg.

(f) The Regulatory Accounts shall set out and reconcile by format, (i) mail volumes derived from revenue data recorded at the point of sale; and (ii) mail volumes based on operational data recorded at the outward phase of the postal pipeline. The Regulatory Accounts shall also clearly explain, by format, the reasons for any divergence between the two mail volume measures.

4.1.4 Cost Allocation and Apportionment Principles

4.1.4.1 The Regulatory Accounts shall, within the operating segments as defined by IFRS 8, allocate costs to each service (i) which is part of the universal postal service and (ii) which is not part of the universal postal service, in the following manner:

(a) a cost which can be directly allocated to a particular service shall be so allocated;

(b) a common cost which cannot be directly allocated to a particular service shall be allocated as follows:

(i) whenever possible, the common cost shall be allocated by direct analysis of its origin;

(ii) when direct analysis of the common cost's origin is not possible, a common cost shall be allocated on the basis of an indirect linkage to another cost category or group of cost categories for which a direct allocation is possible; the indirect linkage shall be based on comparable cost structures;

(iii) when neither of the methods in (i) or (ii) will work, the common cost shall be allocated on the basis of a general allocator computed by using the ratio of all expenses directly or indirectly allocated, on the one hand, to each of the universal postal services and, on the other hand, to the other services.

(iv) common costs, which are necessary for the provision of both the universal postal services and non-universal postal services, shall be allocated appropriately; the same cost drivers must be applied to both universal postal services and non-universal postal services.

4.1.4.2 Costs shall, at a minimum, be allocated to each service in such manner as to ensure that the following activities can be calculated:

(a) Revenue Collection;

(b) Collection;

(c) Outward sorting;

(d) Transport;

(e) Inward sorting; and

(f) Preparation and Delivery.

4.1.4.3 The accounts shall also distinguish between: directly allocated costs and indirectly allocated costs.

4.2 Cost-orientation for each respective price of the universal postal service

4.2.1 In accordance with section 28(1)(b) of the 2011 Act, the Regulatory Accounts shall demonstrate how each respective price of the universal postal service prices is cost-oriented.

4.3 Ad hoc reporting

4.3.1 The USP shall prepare and provide such *ad hoc* reports as may be required by ComReg, from time to time, and any such report may be subject to an Agreed Upon Procedures.

4.4 Balance sheet reporting at regular intervals

4.4.1 If the cash at bank and in hand of the An Post Company's should fall below €100 million, the USP shall report in writing the An Post Company balance sheet at quarter end to ComReg within four weeks of the end of each quarter (i.e., within four weeks of the end of March, June, September, and December).

5. ACCOUNTING MANUAL

5.1 The Accounting Manual shall set out the processes and policies used to prepare the Regulatory Accounts, to include the processes used to calculate the mail volumes and revenues, by service (being the revenue-derived and operational-based mail volumes and revenues, machine counted and manual counted).

5.2. The USP shall

a) review the Accounting Manual annually;

b) make the Accounting Manual available for audit by the Regulatory Auditor and provide any information that the Regulatory Auditor may require to conduct its audit; and

c) inform ComReg in writing of any changes to the Accounting Manual.

5.3 The Accounting Manual shall contain a schedule showing how each cost category shall be treated.

5.4 The Accounting Manual shall provide a sufficiently detailed overview of:

a) The USP's businesses and services, explaining the main activities and functions performed by An Post to deliver postal services to customers, and clearly indicating which businesses and services are regulated;

b) The USP's management structure;

c) how the underlying financial transactions which support the USP's business activities and functions are recorded in its financial ledgers and how transactions are grouped to provide the starting costs, revenues, assets and liabilities used within the internal costing systems to allocate costs;

d) The USP's accounting systems, in terms of the underlying costing principles and the conceptual flow of costs and revenues from source financial systems to the separated businesses;

e) what the Regulatory Accounts comprise and the regulatory accounting process (including the basis of preparation for the Regulatory Accounts);

f) any year-on-year changes to the Regulatory Accounts and/or to cost allocations, together with an assessment of the impact of these changes;

g) how the Regulatory Accounts differ from the Statutory Accounts;

h) the internal safeguards incorporated to ensure that the cost allocation system is free from material error;

i) how operational-based mail volumes are calculated (this should include details of how machine counts are validated and the degree of accuracy to which machines are tested. For manual counts, this should include details of how average container fills figures are reviewed each quarter basis and what the resulting figures are);

j) The Accounting Manual shall include a list of the Services which may be published by ComReg.

5.5 Cost allocation and apportionment rules

5.5.1 The Accounting Manual shall set out how the cost of the various aspects of providing services shall be identified.

5.5.2 The Accounting Manual shall set out how the cost of the various aspects of providing services are apportioned between services. Costs shall be apportioned between the various services that use each aspect of the network on the basis of cost drivers which reflect the different impact of each postal packet on the cost of the activity.

5.5.3 The Accounting Manual shall set out:

a) the processes by which the USP shall distinguish between costs which can be directly assigned to particular services, or indirectly assigned, or assigned as a common cost;

b) the processes by which the USP identifies avoidable, variable, and fixed costs, including detailed worked examples;

c) how equivalent volume drivers, if used, shall be derived;

d) how costs shall be allocated to services with different weight, format, and payment characteristics;

e) how costs shall be allocated to services with different tariffs;

f) a detailed explanation where weight factors used in the allocation process do not align with the various tariff price points; and

g) how cost drivers are reviewed, updated and verified, in particular the nature of, and reason for any year-on-year change in the methodology of cost driver(s), including the reasons why any prior-year adjustment to the Regulatory Accounts has, or has not been, made.

6. REVIEW AND CONFIRMATION OF COMPLIANCE

6.1 The USP shall provide its Accounting Manual and Regulatory Accounts to ComReg within 10 weeks of the end of its financial year. Both documents will then be audited by the Regulatory Auditor and the USP shall provide any information that the Regulatory Auditor may require in order to conduct its audit.

6.2 The Regulatory Auditor shall audit the Accounting Manual and Regulatory Accounts on a present fairly basis.

6.3 The audit shall include a review of:

a) the revenues, costs, and volumes included in the Regulatory Accounts;

b) the reconciliation between the Regulatory Accounts and the Statutory Accounts;

c) the correctness of figures, including operational volumes and the reconciliation of revenue-derived volumes to operational volumes;

d) methodologies used regarding amortisation, cost capitalisation, and cost allocation (including Transfer Charges for Inter-company transactions and Inter-segment transactions);

e) appropriateness of the usage of the cost drivers;

f) nature and detail of all transfer charges / inter-company / inter-segment charges;

g) the frequency of updates used for cost allocation purposes;

h) appropriateness of any changes in the cost allocation methodology; and

i) whether the Accounting Manual continues to fairly present the USP's processes, procedures, and policies in preparing the Regulatory Accounts.

6.4 The USP shall make available all information that the Regulatory Auditor may require to conduct its audit, including any statistical sampling used to identify mail volumes subject to (i) annual statistical review; and (ii) annual procedural review, taking into account changes to the population size of each service, or other significant market changes. The statistical and procedural reviews shall be audited by ComReg or a competent body appointed by ComReg. Any alterations to the procedure resulting from the review shall be stated in the Accounting Manual.

6.5 Where the Regulatory Auditor requires any amendment or correction to the Regulatory Accounts or Accounting Manual, the USP shall do so within a time period set by ComReg.

6.6 Upon completion of the audit by the Regulatory Auditor and the making of any required amendments or corrections by the USP to the Regulatory Accounts or Accounting Manual, the Regulatory Accounts and Summary Regulatory Accounts shall include the report and opinion of the Regulatory Auditor on the USP's compliance with this Direction.

7. STATUTORY POWERS NOT AFFECTED

7.1 Nothing in this Direction shall operate to limit ComReg in the exercise and performance of its statutory powers or duties conferred on it under any primary or secondary legislation (in force prior to or after the Effective Date of this Direction) from time to time.

8. TIMETABLE

8.1 This Direction will apply to accounting periods beginning on 1 January 2017.

8.2 The USP is further required under this Direction to submit its timed programme for compliance with this Direction to ComReg, for ComReg's review and approval, by 1 July 2016.

9. MAINTENANCE OF OBLIGATIONS

9.1 If any section, clause or provision or portion thereof contained in this Direction is found to be invalid or prohibited by the Constitution, by any other law or judged by a court to be unlawful, void or unenforceable, that section, clause or provision or portion thereof shall, to the extent required, be severed from this Direction and rendered ineffective as far as possible without modifying the remaining section(s), clause(s) or provision(s) or portion thereof of this Direction, and shall not in any way affect the validity or enforcement of this Direction or other Directions / Decision Instruments.

10. EFFECTIVE DATE AND DURATION

10.1 This Direction is effective from [DATE], and shall remain in full force unless otherwise amended by ComReg.

[]

Commission for Communications Regulation

Dated []

Q. 4	Do you have any comments on the draft Direction? Please explain your response and provide details of any amendments that should be considered by ComReg.

7 Conclusion

204 Having regard to the applicable statutory provisions of the 2011 Act, this consultation set out ComReg's preliminary views on the universal postal service accounting obligations and updating the Accounting Direction pursuant to section 31 of the 2011 Act. For the most part ComReg's preliminary views are continuations of the existing requirements of the 2006 Accounting Direction. However, ComReg's preliminary views also include proposals for additional information to be provided by the USP in its Regulatory Accounts in order to enable both ComReg and the USP to discharge its respective obligations under the 2011 Act. Where ComReg is proposing that additional information is provided by the USP, ComReg is of the preliminary view that these are proportionate and ComReg has endeavoured to ensure that these additional requirements are fully capable of being implemented by the USP and at no or minimal additional cost as such information is already produced, in full or in large part, by the USP's current cost accounting system / other information systems.

205 ComReg will consider all submissions to this consultation, together with any other relevant evidence, in finalising its positions on the universal postal service accounting obligations.

Submitting comments

The consultation period will run until 5pm on 27 January 2016, during which time ComReg welcomes written comments on any of the issues raised in this consultation.

It is requested that comments be referenced to the relevant question numbers and paragraph numbers from this document. Where views are provided, please provide a supporting rationale for your comments, including if possible, an indication on the broader impact of any changes updated.

As it is ComReg's policy to publish all responses in order to make them available for inspection, responses to consultations should be provided as non-confidential documents, with any information for which confidentiality is claimed (e.g. commercially sensitive information) supplied in a separate annex. In this respect, please refer to ComReg's Consultation Procedures - ComReg 11/34 and ComReg's guidelines on the Treatment of Confidential Information - ComReg 05/24.

We request that electronic submissions be submitted in an unprotected format so that they can be appended into the ComReg submissions document for publishing electronically.

All responses to this consultation should be clearly marked:- "Reference: Consultation 15/135", and sent by post and/or e-mail to arrive on or before **5pm, 27 January 2016**, to:

Mr. Stephen Brogan
Commission for Communications Regulation
Abbey Court, Block DEF
Abbey Street Lower
Dublin 1
D01 W2H4

Email: marketframeworkconsult@comreg.ie

Questions

Section Page