



UNIVERSAL POSTAL UNION

Presentation to the IPC shareholders meeting

Benchmarking postal regulator effectiveness

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BENCHMARKING POSTAL REGULATOR EFFECTIVENESS

I very much appreciate this opportunity to make a presentation to the IPC Shareholders Meeting. There has been a long history of productive cooperation and coordination between the IPC and the Universal Postal Union and we look forward to working together to address the challenges that will confront the Posts of the 21st Century.

One process critical to the future of the Posts and to the survival of universal service is the reform of the regulatory regimes used to manage postal marketplaces. I am pleased to mention that the UPU is producing a *Regulation Guide* to serve as a basic framework for future efforts in this area. However, the topic of postal regulatory reform could occupy many days and numerous presentations. Today, therefore, I will briefly focus on one critical aspect of the reform process that is treated in the *Guide*, namely, how to evaluate postal regulator effectiveness. I will do this by covering three sub-topics:

- The need for effective postal regulators.
- Benchmarking effectiveness of postal regulators.
- How the UPU can support reform and modernization of postal regulation.

1 The need for effective regulators

Development of postal market liberalization

The current pace of both *de jure* and *de facto* postal market liberalization was unimaginable just five years ago. On a national, regional, and global level, private operators are playing an increasingly important role in the provision of even the most basic postal services. As just one example of this process, in the Latin America region, incumbent universal service providers (or USP's) have a share of the postal marketplace estimated at less than 40%, in spite of benefiting from some of the highest *de jure* protection in the World. At the same time, many USP's have commercialized their operations and some have even started the process of privatization, all the while attempting to provide a politically acceptable level of universal service. On an international level, national barriers to open competition are increasingly blurred due to intense competition among some public postal operators as well as private operators and, to some degree, in response to pressure from regional and World Trade Organization initiatives.

However, postal market regulation has not kept pace with these developments

In the face of this rapidly growing wave of postal market liberalization, it will be difficult to sustain meaningful levels of universal service **and** simultaneously develop competitive postal marketplaces without efficient regulatory regimes managed by effective regulators. In reviewing the progress of postal regulatory reform, however, one fact becomes immediately rapidly apparent: the definition of the regulator's role in the modern postal market has not kept pace with developments in the market itself.

Regulators in most developing countries and even some industrialized countries are attempting to regulate with processes more suited to the static, monopoly-based postal industry of the past than to the dynamic, multi-operator, customer-driven market of the future. Moreover, the regulatory frameworks supporting these systems frequently do not provide adequate division of responsibility amongst policy-makers, regulators, and operators themselves. The regulator is often part of the same ministry that acts as the policy-maker and represents the government as owner of the incumbent. While this lack of institutional clarity is at least partially due to the slow pace of postal privatization, it also leads to a disproportionate amount of regulator focus (both favourable and unfavourable) on the USP. As a result, significant portions of the market and large numbers of private operators may receive no attention except when they apply for a license. There is a simultaneous lack of transparency in decision-making, resulting in lower regulator credibility and effectiveness, and diminished market development.

The size of this "regulation vs reality" gap differs from country to country and from region to region. Clearly, the European Community, under the simultaneous guidance and spur of EC postal directives, has made some notable progress in defining regulator responsibilities and enacting supporting legislative frameworks. In other regions, this progress is more modest. A recent survey showed that while in 31 out of 46 African countries significant USP commercialization has been achieved, in 31 of these countries, the postal regulator was still a government function working in the same ministry.

From an operator's viewpoint, improving the effectiveness of these regulators is an essential element to ensuring the future maintenance of universal service in an increasingly liberalized postal market. Therefore, it is important for operators to understand how to evaluate regulator effectiveness and how to benchmark the performance of any given regulator against international best practices.

2 Benchmarking effectiveness of postal regulators

Evaluating and benchmarking regulator effectiveness requires a standard structure and indicators through which any and all postal regulators can be evaluated. While a wide variety of approaches and elements could be used, a useful point of departure is the benchmarking tools that the World Bank Group and other organizations use to evaluate analogous infrastructures such as telecommunications. The goal is similar, namely to determine whether the regulatory function is appropriately situated and structured to fulfil its role and responsibilities. The basic elements for benchmarking are shown in Exhibit 1. By "postalizing" each of these, it is possible to identify existing impediments and potential improvements to improve regulatory effectiveness and impact.

Let us look at each element in more detail.

Legislative foundation

The effectiveness of postal regulators depends first on the existence of a sound postal legislative foundation. The basic regulatory elements, from an operator's viewpoint are relatively standard:

- Clear definition of the postal market in terms of postal items and processes.
- A quantifiable USO definition in terms of coverage, access, price, and quality.
- Identification of the USP responsible for providing this service and the means for financing it (reserved service, universal service fund, direct subsidy, and least subsidy schemes through which unprofitable portions of the network are bid out and awarded to the lowest bidder (e.g. a bus company).
- A strong institutional foundation (e.g. government owned corporation) for the USP.
- Clear demarcation of reserved and competitive areas and "rules of game" for participating in each.
- Definition of distinct responsibilities and transparent processes for the policy setting, regulatory and operational activities.
- If liberalization is specified in the legislation, a clear path and milestones to achieving it.
- A commitment to comply with international obligations.

The legislative foundation should be supplemented with a *sector policy* that states the government's strategic decisions and goals concerning market structure, competition, growth, economic contribution, social objectives, etc. This policy should be forward-looking and immune to political changes.

Mandate

Once the basic framework exists, the details of the regulatory function can be provided in supplementary legislation. To start, it is essential that the mandate of the regulator be clear and detailed. Normally, this will focus on:

- overseeing provision of universal service;
- maintaining a fair and competitive postal marketplace;
- protecting new entrants from anti-competitive practices and predatory pricing;
- ensuring access to the universal service network and interconnection at fair and equitable rates;
- coordinating transparent accounting practices and tariff-setting activities;
- representing consumers; and
- monitoring and stimulating overall postal market development.

The balance amongst these somewhat divergent areas should be clear and ongoing and reflect the regulator's impartiality. As an example, the desire to stimulate competition and guarantee entry and access to the marketplace should not come at the expense of universal service. In fact, ensuring the provision of universal service will typically be the most challenging of the regulator's responsibilities as it involves a large number of individual consumers, political and business interests, and the provision of a basic social obligation in a competitive market. This responsibility will become more challenging as markets grow progressively more liberalized and competitive.

Authority

The regulators' authority to carry out each of these responsibilities should be clear and enforceable. Does the regulator have the authority not only to issue licenses to operators (including the incumbent in competitive areas) but also to impose fines and sanctions and, where warranted, revoke licenses?

To what extent can such decisions be appealed? Is the regulator empowered to resolve disputes among operators? Can the regulator enforce quality of service standards where these apply? To a great extent, the perception and respect granted to the regulator's authority are as important as its definition in law. Unfortunately, in many countries the reluctance of regulators to impose fines and revoke licenses, along with frequent deference to political pressure, have not strengthened this perception.

Autonomy

Independence and insulation from political and business influences are important elements in making and enforcing difficult regulatory decisions. Two elements are critical here: institutional placement and financing. Does the regulator report to an entity separated from policy-making and operator functions? What are the criteria for nomination and dismissal of regulators and their staff? The more removed the regulator is from operator and policy functions, particularly where the policy maker is still the owner of USP, the more transparent and creditable the regulatory process.

To some extent, overall institutional placement will also be affected by the decision whether to have a *sector specific* regulator or rather to have the postal regulator function within a *multi-sector* regulatory environment along with other communications or infrastructure industries. There are clear advantages to the latter approach, based on lower administrative costs, greater opportunities for coordinated ICT development, and the potential for sharing common expertise (e.g. legal). If the multi-sector approach is chosen, it is critical that the postal function receive adequate priority and resources.

The other key issue is financing. Financing can come from the government or from the sector itself through licensing fees, fines, and other administrative charges. Again the principles of separation and transparency would recommend the latter approach. In any case, financing should be free from political and business influence and its use should be controlled by the regulator with accountability provided through external audits.

Transparency

To a great extent, the regulator's success will depend on its ability to receive and process input from all stakeholders, operators, consumers and policy makers. The regulatory process should be participatory and open. Publishing the regulator's decisions and the rationale behind them on an ongoing and periodic basis (for example with an annual report) can build confidence and credibility in the regulator's role.

There must also be an adequate level of predictability in decision-making, particularly in the area of issuing licenses for operators and in enforcing compliance with the terms of these licenses. The conditions for receiving a license must be clear and consistent, and to the greatest extent possible, on terms defined by the regulator itself. While the conditions should be liberal enough to encourage new entrants, the license should contain obligations with enough "teeth" for the regulator to enforce them. Finally, there should be clarity concerning those roles in which the regulator serves as an *advisor* to the policy maker (e.g. the specific parameters of universal service obligations) versus those where it is the *decision-maker* (issuing licenses and sanctions).

Resources and structure

Authority, autonomy, and transparency must be backed up with sufficient resources. These resources involve both specific postal expertise and sufficient numbers of staff to complete regulatory responsibilities. Postal regulatory expertise may not require the same level of technical expertise as other sectors (for example, spectrum management in telecommunications). However, because of the very low barriers to entry, postal regulators must deal with a much larger number of operators, perhaps several hundred as opposed to two or three telecommunications operators. This requires a detailed knowledge of the postal market structure and dynamics.

The key resources are data concerning volumes, revenues, product offerings and prices, areas and hours of operation, etc. Some of this information may be commercially sensitive, and therefore the regulator will have to have both the authority to collect this data and adequate procedures to ensure confidentiality. The regulator also needs comprehensive market data to monitor progress on overall sector development and growth. The monitoring of such sector performance indicators (e.g. market

expansion, per capita mail volumes, cost of service, level of competition, access to service and quality) also demonstrates the impact which the regulatory regime and the regulator are having on overall economic growth and social development objectives.

The size of the regulator's staff will depend to a certain extent on the size and complexity of the postal market. The executive structure of the regulator can take a number of forms including a Board, Commission, etc., supported by the necessary economic, financial, legal or other technical expertise. The distribution of the responsibilities of this staff should be proportional to the task at hand.

Accountability

In the ideal world, there would be no need for a specific postal regulatory regime and postal operators and the postal market would be subject to the same regulations that governed other commercial entities. However, this is not currently the case and postal regulators must have direct accountability to some higher-level function (legislature, courts, etc.). This accountability can be ensured through review and approval of annual reports, external audits, and other documentation, as well as through the authority of this higher level to appoint and dismiss the head and other senior regulator staff for justified reasons. Furthermore, the regulator's decisions must be capable of being appealed through some other impartial system

From all of the foregoing, it should not be assumed that the challenges postal regulators are facing are unique by comparison to their counterparts in analogous infrastructure services. Many telecommunications regulators, for example, face many of the same impediments and constraints in regulating their industries.

Evaluation tool

Exhibit 2 is a graphic representation of the benchmarking process that could be useful in starting the dialogue on how to upgrade regulator effectiveness based on the above discussion, with Argentina and Tanzania provided as specific examples.

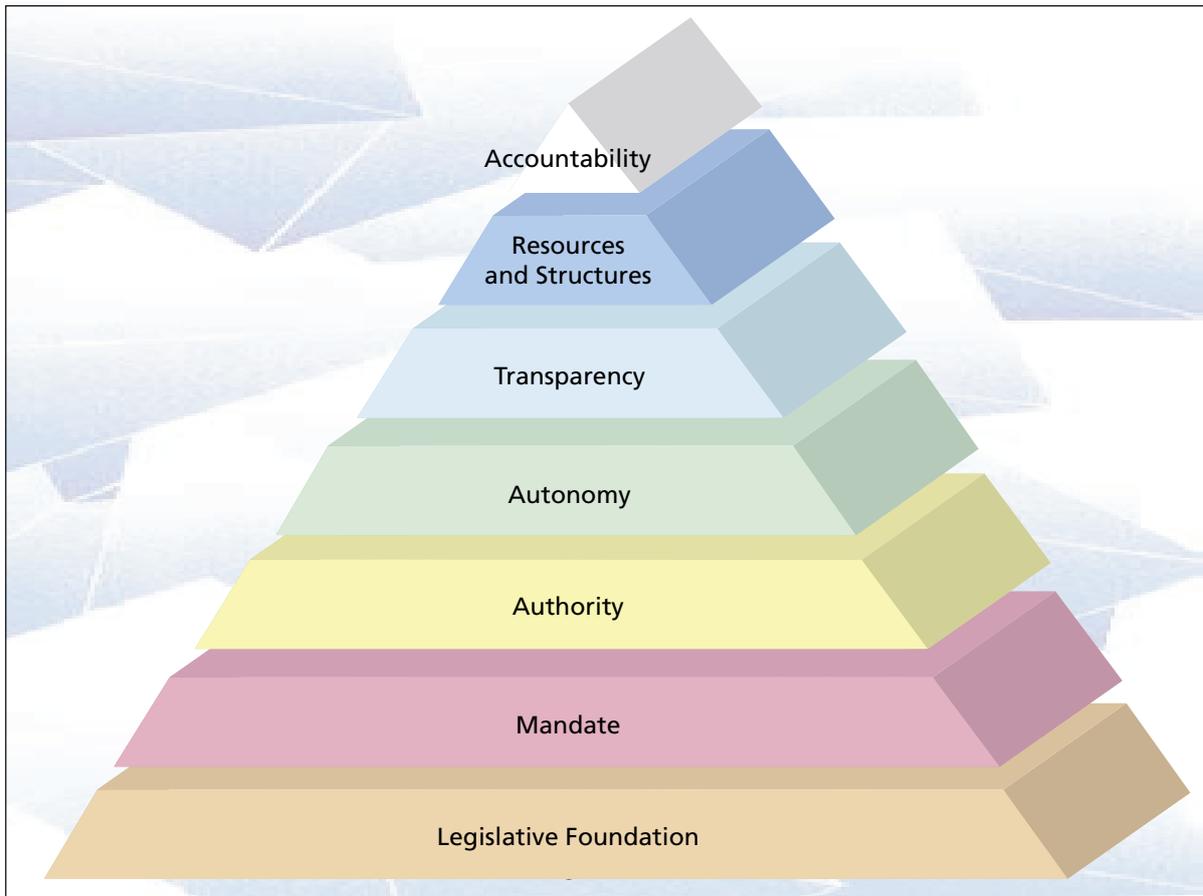
3 How the UPU can support reform and modernization of postal regulation

Let me now turn briefly to my final topic, how the UPU can support efforts to improve regulatory performance. Of course, in the area of harmonizing international regulatory frameworks, the UPU contribution is very familiar. Primary among these is the UPU convention with its regulatory provisions for exchange of international mail along with its terminal dues system which provides the economic framework for reimbursing operators in destination countries for services provided. Another extremely important task is the UPU's effort to promote postal reform by identifying ways in which universal service obligations can be fulfilled in the context of a commercially-oriented business structure. The development of universally acceptable standards, operational procedures and related technical specifications will help lay the foundation for one of the regulator's most basic responsibilities.

A second area is the work that the UPU is doing with its international counterparts, such as the World Bank Group, to develop a series of postal regulatory models and best practice benchmarks. Many of you are involved in analogous efforts as the accession countries work to harmonize their regulatory frameworks with the European Union standards.

The UPU is working to disseminate best practices in these areas through training, seminars, workshops, consultant missions, and development of analytical models such as that shown in Exhibit 2. In an increasingly competitive and interconnected environment, developing such evaluative mechanisms will be an important tool for advancing regulatory harmonization.

Finally, the UPU has, and will continue to serve as an open forum for discussing the most pressing issues and pressures confronting regulators in the international postal market. Whether these challenges involve extraterritorial offices of exchange, cost-based terminal dues, WTO commitments and schedules, or the threats and opportunities posed by electronic communications, the UPU will continue to work with both regulators and operators to design solutions that maintain the viability and integrity of the single postal territory concept.



Basic Components of regulator effectiveness

Exhibit 1

Exhibit 2

Regulator effectiveness indicator	Tanzania	Argentina	Outcome if not present
<p><i>Legislative foundation/sector policy</i></p> <ul style="list-style-type: none"> - market definition - quantifiable USO definition - USO provider/financing identified - institutional definition of provider - clear reserved/competitive line - stakeholder transparency - clear liberalization path - compliance w/internat. agreements 	Present	Present, but inadequate	<p>Ambiguity of regulator role</p> <p>Lack of support for national goals</p> <p>Poor regulator performance</p> <p>Weakening of universal service, universal service provider sustainability</p>
<p><i>Mandate</i></p> <ul style="list-style-type: none"> - USO provision oversight - maintain competitive marketplace - ensure equitable access and interconnectivity - tariff setting for reserved services - represent consumers - monitor market development 	Present	Present, but inadequate	<p>Anti-competitive behaviour</p> <p>Predatory pricing</p> <p>Lack of new market entrants</p> <p>Insufficient competition</p> <p>High cost of service</p> <p>Poor service quality</p>
<p><i>Authority</i></p> <ul style="list-style-type: none"> - issue license on regulator terms - issue fines and sanctions - revoke licenses - monitor quality - settle disputes - provide advice to policy-maker 	Present	Not present	<p>Lack of discipline in issuing licenses</p> <p>Lack of governance and poor enforcement of legislation</p>
<p><i>Autonomy</i></p> <ul style="list-style-type: none"> - distance from other stakeholders - sector specific regulatory approach - objective nomination/dismissal process - funding from independent sources - ability to manage own finances 	Present	Present, but inadequate	<p>Excessive political/business interference with regulator</p> <p>Dependence on non-sector funding</p> <p>Confusion of stakeholder roles/responsibilities</p>
<p><i>Transparency</i></p> <ul style="list-style-type: none"> - participatory approach to regulation - ongoing publication of decisions - explanation of rationale for decisions - consistent licensing policy - consistent application of fines, etc. 	Present	Non present	<p>Lack of explanation for decisions</p> <p>Low regulator credibility and consistency</p> <p>Operator/consumer evasion of regulatory process</p>

Regulator effectiveness indicator	Tanzania	Argentina	Outcome if not present
<i>Resources and structure</i> <ul style="list-style-type: none"> - necessary expertise - sufficient staff - market-responsive internal structure - access to complete market data - sufficient confidentiality guarantees - comprehensive performance indicators 	Present	Present, but inadequate	Inadequate resources and poor performance Lack of market knowledge Inability to track market development and support growth
<i>Accountability</i> <ul style="list-style-type: none"> - higher-level review - appeal process for decisions - audits of regulator finances - periodic and annual reports 	Present	Present, but inadequate	Distrust of regulatory process Ineffective regulation of market

Argentina's postal sector: The cost of regulatory failure.

The outcome of the 30-year concession awarded in 1997 for public postal services of Argentina is unfortunately quite well known, culminating in the recent revocation of the concession by the Government. There were numerous reasons for this failure: overly optimistic postal market growth projections, an unsustainable concession fee (approximately 20% of turnover), and of course, the collapse of the Argentine economy. But the design of an inadequate regulatory framework in one of the World's most competitive postal markets (hundreds of legal and illegal operators) added significant pressures to a difficult situation. The regulator was not empowered to ensure a "level playing field," rarely enforced licensing requirements on private operators, and had assigned nearly all of its staff of 32 regulatory staff to monitor the operations of the incumbent, Correos de Argentina, S.A. Correos faced essentially unregulated competition in a totally liberalized market (since 1993) while trying to meet stringent universal service obligations (no flexibility to adjust service levels or raise prices) and pay up to 60% higher labour rates than private competitors. Finally, there were significant divergences between competition policy and postal regulatory policy, seriously limiting Correos' corporate commercial options for improving its situation. The strategy of initiating liberalization and later attempting to regulate the market had predictable results: Correos' market share plunged from 61% to 38% in the first four years of the concession and the operator eventually was forced to declare bankruptcy.

Tanzania... liberalization following regulatory reform

Tanzania based modernization of its postal sector on a process of regulatory reform starting in the mid-1990's. A sound legislative framework was put in place and an independent and effective regulator, the Tanzania Communication Commission (TCC), was established as part of a multi-sector approach to regulation. A separate body, the Presidential Parastatal Sector Reform Commission was established to oversee market liberalization objectives and the potential privatization of the incumbent, Tanzania Post Corporation (TPC). Clear separation of policy-making, regulator, and operator functions was achieved; TPC signed a performance contract with the TCC and PSRC based on standard performance indicators and featuring financial incentives and penalties. There is transparency in price-setting, USO monitoring, competition, and quality regulatory processes. A reserved area has been maintained to finance universal service obligations but future plans are to reduce this area as TPC gains financial strength. Implementing an effective regulatory regime with incentives and benefits to prepare for liberalization has provided sector-wide benefits in one of the poorest countries in the World. Universal service coverage and TPC's range of product offerings have been expanded. New, licensed competitors have entered the market but TPC has managed to maintain financial equilibrium in a more competitive market.