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DIRECTORATE FOR FINANCIAL, FISCAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

Working Party No. 2 on Competition and Regulation

ROUNDTABLE ON NON-COMMERCIAL SERVICE OBLIGATIONS AND LIBERALIZATION

-- United States --

The attached document is submitted by the delegation of the United States to the Working Party No. 2 of the Competition Committee FOR DISCUSSION under Item VII at its forthcoming meeting on 13 and 14 October 2003.

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II. Comments of General Applicability

6. “Universal service” programs are complex political products. The implicit funding and disbursement methods that historically have characterized “universal service” programs, and often still do, make it difficult for contributors and beneficiaries alike to know with precision how they are affected by the programs, and in many cases, whether they are a net beneficiary or contributor. Regulators seldom study, or publicize, the actual effects of such programs on distribution, penetration, or economic efficiency. Traditionally, these programs have been shielded from a degree of critical scrutiny by the murky cost structure of the regulated monopoly firm.

Impact of Liberalization

7. Where efficient competition is possible, liberalization eventually will strip away the funding from implicitly financed redistribution programs because entrants will offer lower-priced service to the high-margin customers that traditionally provided funding. Alternative funding mechanisms, consistent with competition, become necessary to the extent that pricing structures inconsistent with market-based pricing are to be maintained. In the United States the recent approach under liberalization usually has been to move toward explicit funding of distributional goals. Fees and taxes[2] are levied on entrants and the incumbent alike to the extent they provide the services designated as sources of funding.[3]

8. Liberalization may also call for more explicit and competitively neutral ways of distributing compee0303(lik)1elig(1t)41ib(1t)41l0..9(ely)u(en1)19.5-z 6iz1trk1to 6(’s id(1t)41f)-2.rk1trk1t1t1t1t1tely(t)l2.rk2.9(

11. Although firms may not voluntarily provide the targeted services in question at prices that are set below cost, it does not follow that targeted customers would not buy them or firms would not provide them at prices that did cover economic cost. A number of products delivered as "noncommercial services" likely are "noncommercial" only because their prices are set below cost. Most "noncommercial services" have not been subjected, in modern times, to a market test to determine whether in fact they are "commercial services" that customers would buy, and firms would deliver, if priced at economic cost.[6]

programs seldom target subsidy benefits only or primarily to those who would not otherwise subscribe. (In the case of the hypothetical student, for example, she might otherwise use phone service purchased by her parents, a university, a wireless connection she purchased herself, or a connection shared with housemates.)

13. In the U.S., traditional universal service programs in telecommunications were funded in significant part from elastically demanded products such as access for long distance services and value-added features. This funding substantially and inefficiently reduced demand for these services. Benefits were broadly targeted, with most subsidized individuals likely to be on the phone network in any case. Most of the subsidy effectively went to subscription, a very inelastically demanded product. Some have estimated that the effect of the long-distance to local subscription transfer has been not only reduced efficiency, but reduced telephone penetration as well. Thus the efficiency effects of actual programs, even in network industries, can, on balance, run counter to potential benefits. Others have noted that, historically, it is the failure to pay h-2.3(f3(i)-2.l, sces)-0.2(in t0.6(t)8.3 th)12t thlocb(ur)8.7ls1.2(t)-2.6(t.1(s)-0.5o0.6(t)

by subsidies, to the extent that providers find that distinguishing cost differences is cheap enough to justify the benefits.

- *Choosing an appropriate source of funding for programs affects efficiency in production and consumption (i.e., both technical and allocative efficiency).*

    - Taxing elastically demanded products tends to be socially costly because, other things equal, it distorts consumption more than does taxing inelastically demanded products. In the industries discussed below, demand for subscription tends to be inelastic and demand for utilization is relatively elastic.

    - The set of products available for taxation matters. In general, broadening the set of products that may be taxed will increase the efficiency with which funds can be raised. (Of course if there are sufficient perfectly inelastic demands left to be exploited, increasing taxes on additional elastically demanded products is not efficient.)

    - The availability and use of general revenues for funding may increase allocative efficiency in

21. Liberalization of the electricity sector at the wholesale level is largely under the jurisdiction of the Federal Energy Regulatory Commission (FERC). FERC=s reform efforts continue toward the goal of establishing independent grid operators across the country. Substantial opposition from some state regulators and vertically integrated utilities has slowed the pace of reform at the national level. As in the retail portion of the sector, events in California have undermined confidence in liberalization policies at the wholesale level.

Responses to Questions (Electricity Sector)

Q: Please list the primary telecommunications, post, transport and electricity services that are covered by non-commercial service obligations.

22. In the electric power sector, the primary existing non-commercial service obligations involve subsidies or protective terms-of-service for low-income households.[10] These policies generally are implemented at the state or local government level because jurisdiction over retail electricity sales and marketing is retained by the states.[11] Some of these programs are administered by the states with funding from the federal government. The non-commercial policy obligations include various combinations of reduced rates, explicit subsidies, subsidies for improved insulation and other weather-proofing, prohibitions against discontinuing service during the winter (and/or summer) when extreme temperatures pose a health risk, and arrangements for a Aprovider-of-last-resort@ (POLR) service for customers that cannot or have not reached an agreement with an independent retail marketer.[12] POLR service itself might be interpreted as a non-commercial service obligation when the price of POLR service makes it unremunerative, but another interpretation is that POLR service is a long-term contractual obligation that turned out to be a bad risk for the suppliers involved. All of these policies except POLR service were in place before liberalization and most have been continued to various degrees under liberalization.

26. Most commonly, making the payments for these programs explicit has resulted in scaling them back. An exception is consumer education. In most state liberalization programs, substantial customer education programs have accompanied the opening of customer choice programs.

27. In some states, some of the subsidies have traditionally been financed through charitable giving programs operated by the distribution utilities. This aspect of financing for public programs has not been directly affected by liberalization. By far the most profound decisions and effects linking liberalization with non-commercial service obligations have concerned the pricing of POLR services. Most states undergoing liberalization elected to establish fixed, regulated rates for POLR service that were below the pre-liberalization level and that were not closely related to ongoing changes in wholesale electric power prices. These decisions about POLR service pricing were generally developed by liberalization proponents as a means to increase public support for liberalization C retail customers realized an immediate benefit from liberalization.

28. With few exceptions, the state decisions to de-couple retail from wholesale prices have had unforeseen[16] adverse consequences for incumbent firms, entrants, and consumers. In the case of California, the decision to fix retail rates had extremely adverse effects when wholesale prices rose in 2000 and 2001. During this period, California=s wholesale prices rose above retail prices, incumbent distribution utilities (the load serving entities) faced bankruptcy, efficient retail marketing entrants could not profitably enter or continue to supply the market, and consumers faced blackouts as supplies shrank while demand continued to grow. Eventually, the state acted to reduce wholesale prices (through long-term contracting) and increase retail prices, but this intervention proved to be a costly policy step as well. While the effects of fixed POLR prices were not as dire in other states (in large part because other states continued to have long-term supply contracts in place for most power supplies, while California did not), lack of entry and low levels of customer switching are common among the states that adopted customer choice programs. Only recently, as wholesale prices have aligned more closely with retail rates, have retail entry and customer switching resumed in the liberalizing states.

29. Another form of interaction between POLR pricing and market liberalization concerns recovery of stranded costs. Stranded costs are costs of an incumbent, vertically integrated utility that are not likely to be recovered under liberalization, but which would have been recovered under traditional regulation of electric utilities (that is the costs were prudently incurred and, therefore, allowed to be included in the rate base). In several states, stranded costs were found to be large. Incumbent utilities offering POLR service may have had incentives and the ability to discourage efficient entry by setting artificially low prices for the energy portion of the retail customers= electricity bills. They could afford to do this because they were allowed to make up for these low energy prices by correspondingly higher billings for stranded cost recovery.[17] Entrants compete against the POLR supplier on the basis of the prices for the energy portion of the bill and do not have access to the compensatory stream of stranded cost payments. Consequently an artificially low energy price for POLR service may exclude efficient entry at little cost to the incumbent firm offering POLR service. This pricing distortion may have contributed to the low entry and switching rates in some states undertaking liberalization.

Q: Have non-commercial service obligations changed with privatisation? Please discuss the role of privatisation in the definition and financing of USO=s.

30. Privatization has not played a significant role in financing the USO because the vast majority of electricity industry assets are and have been privately owned. The most important changes that have accompanied liberalization have been in the sources of funding for the non-commercial service obligations. As described earlier, in most states with liberalization policies, financing of public programs has become more transparent. Charges for these programs now often appear as separate lines on the customers= electricity bills.

38. To the extent that subsidies do more than internalize positive externalities, they may create incentives that result in inefficient decision about location, activities, and investments. News media attention is sometimes drawn to extreme examples of these inefficient incentives at work.

Q: Entry barriers. Does establishing a USO occur in conjunction with entry restrictions that exclude competitors from part or all of a market? Is the argument based on cream-skimming concerns? If

Q: Selection of universal service provider. The provider of a universal service, such as public phone service, can be selected by legislation, by a regulator, or by a bidding process. Are there any other mechanisms that are used? Generally, how is the provider of a universal service selected? Is the

54. POLR service rates are regulated rates based either on legislative determinations of the price (i.e., 10% less than the regulated rate prior to liberalization) or an updated cost-based determination.[28] Where the POLR rate has fallen below wholesale costs, POLR suppliers have often sought to increase the POLR rates. Such efforts have met with mixed responses from regulators and legislators.

Q: If the universal service provider receives a payment, how is the decision made of whether a universal service will be paid for through general taxation or taxes on users of related services?

55. Because subsidies for low-income customers were previously imbedded in the regulated rates, there has been a general assumption that these programs will continue to be paid for by taxes on electricity consumption or by charitable giving.

Q: For universal services that are paid for by general taxes, are the costs of rural customers USO obligations paid by the federal government, regional or local authorities? Might it be more efficient to allow the local authorities to choose (and subsidize) the level of services than for the federal authorities to do this? Why or why not? What are the problems with local authority payment? What are the benefits?

charges for these related services now appear as separate lines. The economic efficiency impacts of such programs typically are not quantitatively considered.

65. Retail rates differ by service territory. In states where the retail rates are bundled and regulated, the rates reflect average costs in the area served by a particular retail distribution utility. Under traditional regulation, historic costs over a year or more are averaged to determine regulated rates in the electricity sector for the next time period. Sometimes there is a fuel price adjustment clause that allows more frequent adjustments to rates. The costs considered in bundled rates include generation, distribution, transmission, billing, and marketing. The range of average retail prices in different states is considerable ranging from slightly more than \$0.04 per kilowatt hour (Idaho) to over \$0.14 per kilowatt hour (Hawaii).[31] In states where the retail rates have been liberalized, retail marketers are allowed to charge rates that reflect their costs and the extent of retail competition; however, in many states the POLR price acts as a de facto cap on prices for all marketers. As described earlier, the POLR prices were at or below average wholesale prices for much of the past three years. Once POLR service is no longer offered or once POLR prices have been adjusted to reflect the costs of POLR service, competition between retail marketers will determine retail prices in the liberalized states.

66. FERC proposes to give merchant transmission projects a prominent role in efforts to increase transmission investment. To date, only a few such projects have been started or proposed. Efforts to undertake merchant transmission projects may be inhibited by difficulties in obtaining siting authority for such projects. Further, the potential use of eminent domain power to obtain land for merchant transmission projects is unclear. Without eminent domain authority, the costs of merchant transmission projects may be greater than those for the same project conducted by a distribution utility using eminent domain authority.

67. Distributed generation connections to the grid or distribution system have been the subject of intense regulatory reform efforts in recent years. Both FERC and the states are working to standardize interconnection procedures for DG. These efforts recently were boosted by issuance of an IEEE standard for connecting small DG units to the distribution system. A remaining issue is the pricing of retail backup service for customers with DG units. Advocates of DG argue that back up services have been priced too high because these prices may not adequately reflect the statistical unlikeliness of simultaneous reliability problems among DG units.

IV. Postal Services

Postal Sector Background Notes

68. From the Revolutionary War period until 1970, the United States Post Office, the predecessor to the United States Postal Service (USPS), was a cabinet level department of the U.S. government. After 1970 it became an independent establishment of the executive branch charged with financing its own operations and providing postal services to the nation in a business-like manner. The 1970 reforms were

69. The universal service obligation (USO) of the USPS requires that the Postal Service shall provide

75. The PRA requires that the Postal Service "shall provide prompt, reliable, and efficient services to patrons in all areas and shall render postal services to all communities."[43] Congress has also directed that "[t]he Postal Service shall serve as nearly as practicable the entire population of the United States."[44] Further, the Postal Service is obligated to maintain a maximum degree of postal services to "rural areas, communities, and small towns where post offices are not self-sustaining."[45] To protect small communities from large-scale closings or consolidations of post offices, the Act stipulates that small post offices cannot be closed "solely for operating at a deficit."[46] If the Postal Service seeks to close an office, it must provide advance notice to customers and its decision to close the office is subject to appeal to the PRC.[47]

76. The PRA also requires that the Postal Service provide a basic letter service at a uniform rate. In particular, the Postal Service must maintain at least one class of mail for letters for which the rate "shall be uniform" throughout the United States.[48] The Postal Service offers a uniform domestic First-Class Mail rate for all mailable articles, currently $0.37 USD for the first ounce (approximately 28.4 grams), regardless of distance. Uniform rates for First-Class Mail are available for articles weighing 1 pound (0.454 kg.) or less; for articles weighing in excess of 1 pound, the First-Class Mail postage rates become distance-related up through 70 pounds (31.8 kg.).

77. The Postal Reorganization Act does not quantitatively address the issue of frequency of mail delivery service. Nevertheless, in response to concerns raised in the early 1980s that the Postal Service might deviate from long-standing policies, annual postal appropriations bills since that time routinely have required that six-day-a-week delivery continue at not less than the 1983 level.

78. Other obligations imposed upon the Postal Service are designed to achieve social policy objectives. The PRA establishes that the Postal Service must offer qualified nonprofit organizations reduced rates for mailing advertising matter, periodicals, and newspapers. Books, educational materials, sound recordings, and films must be carried at uniform rates.[49] Library Mail is also entitled to preferred rates. In addition, the Act entitles blind persons and certain members of the armed forces to mail articles free of charge.[50] The PRA further directs the PRC to consider the educational, cultural, social, and informational value ("ECSI value") of the mail in setting overhead cost assignments for purposes of rate recommendations.[51] As a consequence, mail matter having a high "ECSI value", such as Periodicals, has

closer to its ultimate destination. This program has resulted in the effective privatization of approximately $15 billion of the postal market.

Q: Have non-commercial service obligations changed with privatization? Please discuss the role of privatization in the definition and financing of USO=s.

81. "Privatization" has not occurred explicitly in the postal sector. Several developments have been of interest, however. First, in 1979, the Postal Service promulgated suspensions to enforcement of the general provisions of the Private Express Statutes (PES)[53] thereby allowing private carriage of "extremely urgent" letters.[54] This suspension opened the expedited document delivery market to private competitors. As a result, private suppliers have reduced the share of the expedited service market supplied by the USPS. United Parcel Service and Federal Express are two of the most prominent suppliers that displaced the ab TTj /ly=

Q: Definition of universal service. The precise definition of a universal service can often play a significant role in determining who can provide the universal service. Some definitions are physical, such as fixed line access to a general telephone network, and other definitions are conceptual, such as a service that allows for the connection of a user to the general telephone network from a fixed location. Sometimes definitions are enshrined in law, and difficult to change, and at other times they are enshrined in regulations, and easier to change. How are services defined B in physical or conceptual terms? Are efforts made to define services so that multiple companies could provide

94. The Postal Service's revenue requirement, and consequently rates, are based on a thorough examination of the projected costs, including the expected labor costs for a representative year. Rates are designed to meet the statutory "break-even" requirement in this year. While the revenue requirement and consequently rates are based on estimates of actual costs (not hypothetical "efficient" costs) all expected cost-efficiencies and productivity improvements are incorporated into cost estimates.

100. Commercial advantages that would attach to the provider of universal service if entry restrictions were removed is among the major issues involved in current policy debates regarding the USPS. Since there have been no pilot programs and the promotional efforts of entrants or the USPS under these circumstances are unknown, evaluation is necessarily limited.

Financing (Postal Sector)

Q: Are there any general government policies with respect to the financing of USOs? Examples might include internal financing within the firm or financing through general taxation. When the cost of USOs is calculated, are competitors required to participate in its financing? What mechanism is used to calculate the contribution of competitors? If market share is involved, how is each market participant share calculated?

101. The government policy for financing the postal USO is through the operator's self-sufficiency, but with allowance for limited borrowing from the government during deficit years between rate cases. There is no compensation fund obligating private carriers to support universal service in the United States.

Q: If the universal service provider receives a payment, how is the decision made on whether a universal service will be paid for through general taxation or taxes on users of related services?

102. The explicit subsidies for subsidized mail services, such as mail for the blind and overseas voting materials, are relatively small. The USPS submits information to the administration and to Congress about the costs of funding these mail services. The subsidies may or may not cover the full costs.[82]

Q: For universal services that are paid for by general taxes, are the costs of rural customers USO obligations paid by the federal government, regional or local authorities? Might it be more efficient to allow the local authorities to choose (and subsidize) the level of services than for the federal

available to all citizens at reasonable prices. These twin goals of ubiquity and affordability, however, evolved over time. As early as the beginning of the twentieth century, AT&T, then an emerging monopolist, advocated that a single integrated telephone network should serve the entire nation.[94] Critics argued that AT&T desired to promote industry consolidation and thwart independent rivals. This policy changed during the 1970s when AT&T, the incumbent monopoly provider, faced growing competition in the long distance market. During that time AT&T supported a universal service policy that was designed to defend its status as monopoly provider by advocating ubiquitous access to basic telephone service for all rather than interconnection between competing networks.[95]

116. Historically, universal service consisted principally of a number of implicit subsidy mechanisms at the state and, to a lesser extent, federal levels designed to lower costs for rural service at the expense of urban customers, lower costs for residential service at the expense of business customers, and lower costs for local service at the expense of long distance service. For example, during this period, most states had local rate levels that required businesses to pay more on a per-line basis for local service than residential customers paid for similar service. Moreover, most state regulators set rates for vertical services such as touch tone, conference calling and speed dialing, so that these ancillary services would also subsidize basic residential local service.[96]

including in some instances, access to 911 and enhanced 911 (E911) services; access to operator services; access to inter-exchange services; access to directory services; and toll limitation services for qualifying low-income consumers.[98] Although access to the Internet is not part of the core services, access to advanced telecommunications and information services including access to the Internet is included in the category, technical and service standards, and equal access.[102] The FCC decided to retain the current list of core services eligible to receive universal service support since the additional services that were considered failed to meet the criteria for adding new services that were established by the 1996 Act.[103]

Q: Have non-commercial service obligations impacted efforts at liberalization? Please discuss how, in liberalizing industries, USOs have been met.

127. The liberalization provisions of the 1996 Act made certain of the previously implicit subsidies transparent without affecting the scope of the obligations. One direct impact of this change is that the federal charges for universal service are clearly identified on consumers' monthly telephone bills.[104] However, liberalization affected the pricing of core services supported by the universal service fund. For example, as a result of reform at the federal level of access charges (i.e., charges levied on long distance companies for access to the local loop), the implicit subsidies from long distance to local users have been replaced by an explicit interstate universal service support mechanism. More specifically, access reform reduced the non-traffic sensitive portion of interstate access charges and encouraged local telephone companies to recover these charges through a flat rate charge on local service.[105]

128. In contrast to access reform and lower long distance rates, analysts point out that many states

Q: State whether universal service access is also considered as an option. For example, with Internet service, a user can go to an Internet café to access the network or stay at home. Staying at home requires access to a computer, which many disadvantaged consumers do not have. Thus,

141. Although concerns have been raised by incumbents regarding cream-skimming by new entrants, the requirement that eligible carriers offer the supported services throughout the service area to some

for eligible services. The services considered eligible for support under this program include telecommunications services, Internet access, and the installation and maintenance of internal wiring and connections. Selection of providers is based mostly on price, i.e., low bidder usually wins, but other factors such as prior experience, personnel qualifications, and management capability, are sometimes also used to determine the winning bidder.

Q: Benefits to provider of universal service. Does the provider of a universal service receive any explicit payment for the provision of that service? If so, how large are the payments? Must the universal service provider demonstrate that it provides the services at a non-commercial rate?

144. Generally, any carrier designated as eligible to participate in any of the four universal service support programs -- high cost, low income, rural health care, and schools and libraries -- can receive payments from the universal service fund. Size of the payments depends on the cost of providing the service.

Q: On what basis are costs calculated for USO provision? Are the costs used historical? Are the costs forward-looking? Are models used to estimate the costs? Are these engineering models, as perhaps for telephone and electricity services? Are these process models, as might be appropriate for

Financing (Telecommunications Sector)

Q: Are there any general government policies with respect to the financing of USO's? Examples might include internal financing within the firm or financing through general taxation. When the cost of USO's is calculated, are competitors required to participate in its financing? What mechanism is used to calculate the contribution of competitors? If market share is involved, how is each market participant's share calculated?

147. Telecommunications carriers that provide interstate telecommunications services are required to contribute to universal service. These carriers, however, are not prohibited from recovering their contributions from their customers in an equitable and nondiscriminatory manner. Contributions to the universal service fund are based on carriers' interstate and international end-user telecommunications revenues. Carriers submit their revenue data quarterly. The Universal Service Administration Company (USAC), a third party administrator of the universal service fund, submits demand information for each of the four programs and industry revenue information. The FCC then derives a contribution factor, which is basically total program demand divided by total industry revenue. USAC applies this quarterly contribution factor to each individual carrier's revenue and bills each carrier for that amount. All telecommunications carriers, including both incumbents and competitors, with revenue from interstate and international end users are required to contribute to the universal service fund. The FCC is reviewing the current revenue based assessment system in light of a changing marketplace. New funding proposals

NOTES

1 These materials, organized by Kirin Duwadi, Ph.D., Economist, U.S. Federal Communications Commission, (kduwadi@fcc.gov); John Henly, Ph.D., Economist, U.S. Department of Justice, (john.henly@usdoj.gov); and John C. Hilke, Ph.D., Economist and Electricity Project Coordinator, U.S. Federal Trade Commission, (jhilke@ftc.gov), reflect current US practice, but should not be construed to hold any of the FCC, DOJ, FTC or any other U.S. government entity to a prescribed future course of conduct.

2 We use the terms “fees” and “taxes” interchangeably here whether levied by a regulator or another body. Regardless of who levies the amount, if a fee or tax forces price away from marginal cost, the effect, depending on the elasticities of demand, is to distort consumption and create deadweight losses.

3 A second approach, where a legal or de facto monopoly still exists on a service, or on a critical input to the service, is to permit part of the value-added to be provided competitively while the monopolist continues to provide the critical input or service at a price high enough to fund redistribution programs. Global price-caps and avoided-cost pricing or ECPR are examples. This is closer to the approach taken with postal services in the United States.

4 Another approach to benefits is to procure certain universal services by auction where ex post competition is not possible.

5 In many instances, the size of these programs inadvertently grew beyond the original expectations of proponents since the size and growth of the programs was not transparent. Liberalization served in these cases as an opportunity for public officials to revisit policy areas that had been relatively dormant for many years.

6 The relative success of privately supplied mobile services, normally without universal service funding, is at least a cautionary tale about the impact of some wireline pricing practices designed with the politics of distribution, not economic cost, in mind. In much of the developing world state owned telcos provided residential wireline service that was administratively rationed, far from universal, and sold at prices held below cost by the politics of distribution. Below-cost prices did not provide a sufficient source of investment capital and service to permit the many people willing to buy phone service at economic cost to do so. Many of these people in recent years have purchased unregulated or loosely regulated wireless

11 An instructive insight into state decisions on USO issues is the June 12, 2002, AReport of the Universal Service Working Group@ in Maryland, In the Matter of the Electric Universal Service Program, Before the Public Service Commission of Maryland, Case No. 8903.

12 The public programs of twelve liberalizing states are described in Appendix A of the FTC Staff Report Competition and Consumer Protection Perspectives on Electric Power Regulatory Reform: Focus on Retail Competition, FTC (September 2001). For an early summary of state legislation and state commission policy regarding the scope and design of universal service programs in states with liberalized retail

"The Co-op was organized in 1948 under Title 10-13 of the North Dakota Century Code and is financed by the Rural Electrification Administration in Washington D.C. Under North Dakota law, the Co-op is not

51 39 U.S.C. § 3622.

52 39 U.S.C. §§ 414, 416.

53 In general, the Private Express Statutes (PES), 18 U.S.C. §§ 1693-1699; 39 U.S.C. §§ 601-606, make it unlawful for any entity other than the Postal Service to send or carry letters over post routes for compensation unless postage on the matter carried by private carrier is paid in an amount equivalent to the applicable postage, or the carriage qualifies for an exception or suspension. Thus, private carriage of letters is not prohibited, although, in many circumstances, the PES make private carriage of nonurgent letters economically disadvantageous. For all items, including those that are not considered letters, such as merchandise, newspapers, and periodicals, private carriers may accept and deliver such items, except that, under a provision known as “the mailbox rule,” delivery must be effected through means that do not involve access to mailboxes or post office boxes in Postal Service retail units.

54 39 C.F.R. § 320.6. The President's Commission noted that "some question whether the Postal Service has the authority to define and alter the scope of its own monopoly." President's Commission on the USPS at 24. The Commission also recommended that responsibility for regulating the monopoly should reside with an independent regulatory board. Id.

55 Taking U.S. package delivery as a whole, the USPS share is estimated to be less than 20%. See Alan Robinson, “Competition Within the United States Parcel Delivery Market,” Direct Communications

63 One notable exception to the PES is the private carriage of letters conducted prior or subsequent to mailing. In general, this exception permits private carriage of letters that enter the mailstream at some point between their origin and their destination. Examples of permissible activities under this exception include pickup and carriage of letters that are delivered to post offices for mailing, the pickup and carriage of letters at post offices for delivery to addressees, and the bulk shipment of individually addressed letters ultimately carried by the Postal Service.

64 18 U.S.C. § 1725.

65 There is an active literature on various aspects of the U.S. USO. The literature is reviewed in M. A. Crew and P. R. Kleindorfer, ADeveloping Policies for the Future of the United States Postal Service,@ paper submitted to the President=s Commission on the United States Postal Service (February 20, 2003). Research funding for this paper was provided by the FTC.

66 Cohen, Robert, Matthew Robinson, Renee Sheehy, John Waller, and Spyros Xenakis, "An Empirical Analysis of the Graveyard Spiral", to be published in Competitive Transformation of the Postal and Delivery Sector, edited by M.A. Crew and P.R. Kleindorfer, Boston, MA: Kluwer Academic Publishers, 2003.

67 John Haldi and Leonard Merewitz, ACost and Returns from Delivery to Sparsely Settled Rural Areas,@ in

77 Despite the extent and refinement of the analytical techniques reported by the USPS, concerns have been expressed about the quality of the data used in these analyses and the limited access of the PRC and interested parties to the USPS data and analyses. The 2003 Presidential Commission recommends that the sector regulator be given subpoena authority to better assure the reliability of USPS analysis.

91 There might still be cream skimming in the sense that cost and margin conditions (entry incentives) may differ by route while the fee on private deliveries to mailboxes likely would be set on a system-average basis.

92 Janet Meyers, AFTC Staffer Has Third-Class Idea,@ Advertising Age (March 20, 1989).

93 General Accounting Office, Information About Restrictions on Mailbox Access, GAO/GGD-97-85 (May 1997).

94 Robert W. Crandall and Leonard Waverman, Who Pays for Universal Service, Brookings Institution Press, Washington D.C., 2000; Milton Mueller, Universal Service: Competition, Interconnection and Monopoly in the Making of the American Telephone System, MIT and AEI Press, Cambridge, 1997.

95 Critics argue that AT&T advocated a regulated monopoly regulatory scheme which allowed rate distortions that kept local rates artificially low. See, Crandall and Waverman, and Mueller. Also see, Philip M. Napoli, Foundations of Communications Policy, Hampton Press, New Jersey, 2001.

96 Federal Communications Commission, In the Matter of Federal-State Joint Board on Universal Service, Report and Order, Washington, D.C., May 1997. ("1997 Universal Service Order"). Some analysts have questioned the use of the word "subsidy" to characterize these flows between groups. See, David Gable, "Recovering Access Costs: The Debate," in Making Universal Service Policy, edited by Barbara Cherry, Steven Wildman, and Allen Hammond, Lawrence Erlbaum Associates, Mahwah, N.J., 1999.

97 FCC, Universal Service Order, 1997, p 9.

98 FCC, Universal Service Order, 1997 at p.15.

99 Although TRS is not a part of section 254 of the 1996 Act, which defines federal universal service policy, it provides benefits similar to universal service benefits to a targeted group.

100 International Research Center, "Universal Service to Universal Access", at http://www.researchedge.com/uss/univ_nation.html. Also see, Thomas W. Bonnett, "The new State in Ensuring Universal Telecommunications Services" in Making Universal Service Policy, edited by Barbara Cherry, Steven Wildman, and Allen Hammond, Lawrence Erlbaum Associates, Mahwah, N.J., 1999.

101 General Accounting Office, Federal and State Universal Service Programs and Challenges to Funding, Washington, D.C., February 2002.

102 FCC, Federal-State Joint Board on Universal Service, Order and Order on Reconsideration, July 14, 2003.

103 See section 254(c) of the 1996 Telecommunications Act for the criteria.

104 Telephone companies voluntarily identify these charges in customers' telephone bills.

105 FCC, Access Charge Reform and Order, 1997.

106 See GAO; Bonnett; Gregory Rosston and Bradley Wimmer, "Local Telephone Rate Structures: Before and After the Act", Stanford Institute for Economic and Policy Research, August, 2002. Gable, on the other hand argues that value-of-service pricing is not anti-competitive and that firms regularly price discrim(e)25.4(e, oe, oe, o.1

124 FCC, 1997 Universal Service Order, p. 27.

125 47 Code of Federal Regulations § 54.101.

126 Paul R. Zimmerman, Reference Book.