Neither the Carrot nor the Stick: How to Ensure Adequacy of Traditional Postal Operators' Funding in a Rapidly Transforming Market

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1 Introduction

The postal services market is going through a transformation that is challenging traditional postal operators' ability to meet their universal service obligation (USO). Letter mail decline and increased parcel volume are driving operational changes and costs and re-shaping consumers' behaviors. In order to stay competitive in a rapidly changing market, postal operators need to apply advanced technology solutions to the entire delivery chain while asked to increase efforts to promote sustainable deliveries and reduce environmental impact of their operations. Adapting to the new scenario requires investments in infrastructure and technology to support the delivery of growing parcel volumes and improve customers' shipping experience whilst coping with obligations related to universal service provisions.

As traditional compensation for the cost of universal service provision, as defined in the Postal Services Directive (PSD),[1] cannot sustain these type of investments,

[1] Directive 2008/6/EC of 20 February 2008 amending Directive 97/67/EC with regard to the full accomplishment of the internal market of Community postal services.

How to ensure adequacy of traditional postal operators' funding in a rapidly transforming market

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postal operators are now exploring alternative funding to support their transformation. However, the varied nature of these resources (governmental aids, private financial loans, other funds channeled by the EU recovery plan) and the complexity with respect to their use raise concerns about potential competitive distortions. In this context, it is not yet clear whether EU competition rules, including the EU's current State Aid regulatory framework, would be able to perform a comprehensive scrutiny of those funds and to assess their impact on competition within a rapidly transforming market.

The paper is organized as follows. Section 2 clarifies the relevant changes in the market, and Sect. 3 describes how postal operators are trying to adapt to those changes. Section 4 presents various new forms of financial support that postal operators are seeking. Section 5 explains how these recent developments can result in potential competitive market distortions, assess what methods should be considered to scrutinize new forms of funding for postal operators and advance recommendations to remedy distortions. Section 6 briefly concludes.

2 The Transformation of the Postal Services Market

The decrease of letter mail volumes due to on-going digitization has been continuous and steady in the last decade. At the same time, the increase in e-commerce has driven relevant growth in parcel delivery and is changing the market mix for postal services. This new scenario has two main implications for traditional postal operators: the financial sustainability of the USO becomes more difficult, while the stream of parcel revenues becomes more important to sustain overall operational activity and costs (Romito et al., 2018). Recent studies showed how postal customers' preferences have shifted from mail to parcel items delivery, leading to a gradual transition towards a more receiver-oriented postal market (ERGP, 2020).

In Europe, parcel volumes have increased by more than 30% in between 2014 and 2018. Parcel delivery differs from mail delivery, as it frequently entails more flexible delivery times to either customers' houses or proximity access points. This increase in the volumes of parcels in Europe was triggered by the surge of e-commerce, which resulted especially in a notable increase in revenues from B2C parcels. Many surveys, including one conducted by UPS,,[2] show that online shoppers value the opportunity to choose among a wide range of delivery options, and expect a seamless delivery process, including transparency and real-time updates on the delivery progress. Advanced technological solutions become therefore very important, as access to electronic delivery notifications and track and trace solutions result among most preferred delivery aspects.[3] Customers want flexible and reliable

[2] "Pulse of the Online Shopper – A Customer Experience Study", UPS 2019.

[3] "E-Commerce and Delivery", Copenhagen Economics for European Commission 2013.

solutions for their parcel deliveries and are becoming less and less tolerant when these requirements are not met.

Traditional postal operators, who have seen a progressive erosion of revenues coming from their activity as Universal Service Providers (USPs), have turned to the growing parcel market in an effort to collect additional revenues and keep sustaining their USO obligation. To stay competitive in the parcel delivery market, these operators were pushed to introduce technological innovations and increase operational efficiency in order to provide more customer-oriented delivery solutions at reasonable prices (ERGP, 2020). New strategic plans recently launched by traditional postal operators (e.g. Poste Italiane – Deliver 2022) aim to cope with the increased pressure to deliver parcels efficiently and effectively. In this context, postal operators face also another challenge: the need to deliver postal and parcel items in a more sustainable way. Calls for greener solutions for last-mile delivery to reduce CO_2 emissions are pushing towards the adoption of alternative delivery solutions or the use of alternative fuel vehicles.

Parcel delivery has become even more prominent during the COVID-19 crisis. In a time of lockdowns put in place by European countries, e-commerce has boomed even more, and in the future it is likely that online sales will remain at a higher level than before the outbreak.

3 The Adaptation Process of Postal Operators

3.1 Traditional Postal Operators Explore New Strategies to Stay Competitive

Even in a transforming market, traditional postal operators have to continue meet their USO requirements and guarantee universal service provision at affordable rates. As monitored by the ERGP (2019), letter mail rates actually increased by more than 40% between 2014 and 2018. This price increase has allowed POs to compensate for revenue losses due to declining letter volumes, but it might pose challenges to fair competition within the postal services sector if the trend continues. Significant and constant increases in letter mail rates may generate extra profits that could be used to cross-subsidize other activities, especially the delivery of e-commerce parcel volumes. The phenomenon of cross-subsidization between USO and non-USO services has been investigated in the postal services market and its potential negative effects on competition have been acknowledged.

As per article 7(3) of the PSD, EU Member States can introduce a mechanism to compensate the universal service undertaking when the USO entails a net cost and creates an unfair burden. This mechanism can consist of either a public fund (i.e., a state subsidy) or a compensation fund to be funded by service providers. Despite Article 9(3) of the PSD, which refers to potential contributors to a compensation fund as those “services which fall within the scope of the universal service”, recent rulings of the European Court of Justice (i.e., the DHL Express Austria and Confetra cases) opened the door for Member States to make the grant of general authorizations for postal services delivery conditional on a contribution to a compensation fund.

These rulings make it possible that all postal service providers become eligible to contribute to the fund. Specifically, the PSD states that holders of a general authorization may be requested to contribute to the fund if the services they provide, thanks to such authorization, can be considered as "interchangeable" with the universal service. However, the PSD does not provide clear specifications on how to measure interchangeability between USO and non-USO services, which may raise issues for the breadth and enforcement of the compensation fund. A 2015 report from Copenhagen Economics has developed an interchangeability test that shows how the concept of interchangeability does not properly hold in the postal and delivery services market.[4]

Compensation funds represent State aid measures that can create strong competitive distortions. Fratini and Chovino (2018) indicated how compensation funds can be more distortive for competition than State subsidies, as they combine the effect of benefiting the incumbent with that of weakening its competitors. Another study from Copenhagen Economics (2018) showed how only a few EU Member States have so far introduced a compensation fund[5] and in most of these cases the State is still the main contributor to this fund. In fact, the risk for a compensation fund entirely paid by services operators to alter competition is very high. In short, compensation funds are considered as State aid and have to comply with EU State Aid rules. Their peculiar nature, however, makes it more complex to conduct the State aid assessment.

In order to stay competitive and still meet their USO requirements, traditional postal operators are also exploring mergers with other postal operators. In 2019 PostNL tried to get a license for the acquisition of rival postal operator Sandd, basically the sole other major competitor in the Dutch postal delivery market. The Netherlands Authority for Consumers and Markets (ACM) initially decided not to grant the license as it would have created a monopolist in the postal delivery market.[6] The authority also stated that even if digitization is leading to a decline in physical mail volume, this decline is occurring gradually and PostNL should continue with its postal activities under economically acceptable conditions in the short and long-term. However, in September 2019 the Dutch Deputy Minister of Economic

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[4] "Study on the interchangeability of USO and non-USO services", Copenhagen Economics for the EEA, 2015.The study has marked the first concrete attempt at determining interchangeability of postal services. By departing from an SSNIP test and applying the demand-side framework for definition of relevant markets, the study develops an interchangeability test that shows how the concept of interchangeability does not properly hold in the postal and delivery services market.

[5] "Main developments in the postal sector (2013–2016)", Copenhagen Economics for European Commission, 2018.

[6] "Summary of the PostNL-Sandd Decision", Netherlands Authority for Consumers and Markets, September 2019.

Affairs granted approval of the merger under art. 47 of Dutch competition law, as the combination of the two postal networks was deemed necessary to ensure service continuity.

In Europe, the decline in letter mail deliveries and the related USPs' losses conflict also with delivery frequency requirements. Article 3 of the PSD specifies that the universal service should be guaranteed not less than five working days per week save in exceptional circumstances or geographical conditions. As regulatory obligations for services falling under the USO have remained stable over time, this requirement is now posing great challenges to traditional postal operators and there is a legitimate concern about the ability to meet it in the future.

Recent studies (Copenhagen Economics, 2018) showed that under specific market conditions, reduced delivery frequency to just 2 or 3 days per week could allow USPs to adopt more efficient operational models. This approach can generate cost savings on the delivery activity and these savings can be best reaped when lower delivery frequency is also combined with reduced delivery speed (e.g., moving from the D + 1 requirement to D + 2 or D + 3 as an alternative). However, this approach would fully comply with the current PSD.

Despite providing lower prices and more reliable services to general postal users, these measures could negatively affect those users who still need high frequency of delivery. To address this problem postal operators can also explore hybrid solutions. For instance, the Norwegian universal service provider Posten Norge has reduced its delivery frequency by requiring a standard delivery time of D + 2. It has combined this effort with subsidized express delivery services or monetary compensations to vulnerable users most affected by the frequency change.

3.2 Call for Investments in Physical and Digital Infrastructures

The transformation of traditional postal operators from mail providers into parcel delivery operators is motivated by the need to stay relevant in a postal services market that is now more competitive. New technologies have emerged and their application to the parcel segment of the postal market is playing a critical role in improving parcel delivery efficiency (ERGP, 2020). Postal incumbents have started to focus on the optimization of their operations by investing in all parts of the delivery chain, from sorting, to transport, to pick-up and delivery.

Almost all European main postal operators (e.g., Deutsche Post, Poste Italiane, LaPoste, etc.) have invested in dedicated parcel sorting facilities. These facilities are used for outbound and inbound sorting of parcels and the centralization of sortation allows an increase in the number of parcels processed per location.[7] The steady

[7] "Review of Postal Operator Efficiency", WIK Consult – Study for Ofcom, 2013.

increase in parcel volumes has justified investments into automated conveyor and sortation systems equipped with sophisticated scanning technology.

In a more customer-oriented postal market, new solutions and innovations need to be applied also to last-mile delivery options. Last-mile delivery in e-commerce has evolved rapidly thanks to data analytics, dynamic route optimization, geolocation and connectivity as well as artificial intelligence. Postal operators can now provide more flexible delivery services but the costs of last-mile delivery directly to customers are very high (ERGP, 2020). Even if customers value delivery to their premises the most, operators can achieve cost savings by delivering parcel items to proximity access points. Delivery location becomes very important for customers, together with delivery control and delivery timing.

To balance these aspects postal operators have invested also into automatic parcel lockers (APLs), usually located in public areas accessible all day long. Lockers generate savings in terms of distribution costs and allow to deliver more parcel items. This produces efficiencies otherwise not attainable via traditional delivery services (Scorca, 2018). Proximity access points can also be represented by physical local shops or small businesses. These points are usually located as close as possible to customers' premises and have longer opening hours than traditional post offices. To manage these points postal operators are investing in digital platforms that create an intermediation between the physical proximity points and the customers.

Pressure on postal operators to perform environmentally sustainable deliveries is also increasing (Borsenberger and Joram, 2020). In this case societal pressure is often linked with customers' preferences as more users value sustainability and environmental protection. Many postal operators are now using alternative fuel vehicles (electric vehicles, natural gas vehicles, e-bikes or bikes, etc.) for their last mile deliveries to reduce carbon emissions. Other investments include the use of sustainable packaging and, more importantly, significant investment in more sustainable and energy efficient buildings for distribution centers and parcel sorting facilities. To this end, postal operators are investing in solar panels for energy production, lighting upgrades to achieve energy savings, and power grids to charge e-vehicles. All these investments represent additional costs in addition to those that traditional postal operators have to already sustain to transform themselves into more effective parcel delivery operators and to keep meeting their USO. Moreover, in Europe these efforts are also motivated by the need to comply with the ambitious EU's climate targets. Indeed, through its new Green Deal, the European Union (EU) has committed to achieve carbon neutrality by 2050.

4 Beyond the Compensation Fund for USO

4.1 Alternative Funding to Sustain the Postal Transformation

The provision of financial support to USPs and the need to fund the net cost of universal service obligations (USO) are still part of a debate. The introduction of a compensation fund as an alternative to State subsidy to sustain the USO has raised different views and only one EU Member State, Poland, has so far fully implemented it. As explained by Visco-Comandini (2018), a compensation fund is a tax charged only to competitors for sharing USO costs, while a State subsidy is financed by all taxpayers and allows to share the overall burden more equally within society.

Despite its negative effect on competition, the compensation fund is allowed as a State aid measure that requires ex-ante scrutiny by the European Commission (Fratini, 2016) and whose sole purpose is to compensate the USP for the net cost of USO. The compensation fund is considered as compatible aid provided that there is no overcompensation. However, in a rapidly changing postal market postal operators are now looking at alternative funding to become relevant players in the parcel delivery segment, but the traditional forms of compensation for their USO burden are neither suited nor sufficient to sustain new required investments.

Recent developments in the French postal market provide an example of how local traditional postal operators are trying to access new alternative financial sources to support their operation, and in particular their shift towards increased parcel deliveries. In 2019, the French Minister of the Economy and Finance announced that the French USP LaPoste reached an agreement with the French State, the state-owned investment fund Caisse des Dépôts (CDC) and La Banque Postale for the creation of a large public financial group serving the territories. The creation of this general-interest public group had the goal to strengthen territorial cohesion and address the regional divide throughout the entire country via La Poste and CDC, as services operators serving citizens. The group aimed to offer banking and insurance services suited to the needs of the local public sector, corporates and individuals, thanks to the expertise of La Banque Postale, CDC as well as Bpifrance and CNP Assurances.[8]

To implement the project, both CDC and the French State transferred their respective stakes in the capital of CNP Assurances to La Poste and then to La Banque Postale. Following this transaction, La Poste is now majority owned by CDC, and La Banque Postale's stake in CNP Assurances has increased significantly. As a consequence, the French USP may now have significant additional resources to commit to further investments into the parcel segment of the postal delivery market. This example shows how USPs may obtain access to new funding by replacing

[8] "Signing of a memorandum of understanding between the French State, Caisse des Dépôts, La Poste and La Banque Postale on the project for the creation of a large public financial group", Press release, 11 June 2019: https://le-groupe-laposte.cdn.prismic.io/le-groupe-laposte%2F043294ba-cf9c-429c-9edd-51da0a26deb6_cp-signing-french-state-cdc-glp-lbp-en.pdf

direct State ownership of the aid beneficiary with new intermediary owners, that are in turn owned by the State.

While such cases should be examined under State aid rules, this does not always happen. A recent EU State aid case involving the Nordic postal operator PostNord AB and one of its fully owned subsidiaries, PostNord Logistics, provides instead an example of a situation in which the State used its parent company to contribute cash to its subsidiaries. Following a complaint from the Association for the Danish road transport of goods (ITD) in November 2018, the European Commission examined whether PostNord Logistics (PNL) had received State aid from Denmark and Sweden. PNL is based in Denmark and is 100% owned by PostNord Group (PNG). PNG is, in turn, owned by PostNord AB, whose shares belong to Sweden (60%) and Denmark (40%) while the voting rights are split 50/50. PNG has many subsidiaries of which two are the Danish postal incumbent, Post Danmark and its subsidiary PNL. According to the complaint, State aid had been granted to PNL in three different forms: (i) through the public announcement of an intended capital injection to PNL by PNG; (ii) through an actual capital injection by PNG; and (iii) through the cross-subsidisation of PNL's costs by another subsidiary in the group, Post Denmark. The latter allowed PNL to use its facilities (e.g. trucks, staff, warehouses) which were funded by the USO compensation to Post Denmark.

Per EU State aid rules, even when funds for a project do not come directly out of the State budget but from a publicly owned undertaking, such as PNG, they can still be considered to be State aid if the funds are under the control of the State and the decision to grant the funds can be imputed to the State. Therefore, in this case the Commission had to assess whether investments by a state-owned postal company, PNG, into PNL constituted investments through State resources and whether they could be imputed to the Danish and/or the Swedish states. In May 2020 the Commission concluded that no State aid had been granted to PNL because, even though PNG via its parent PostNord AB is 100% owned by the Danish and Swedish states, and this implies the use of State resources, the capital injection by PNG to PNL could not be imputed to the Danish or the Swedish states.

The Commission decision stated that a measure cannot be imputed to the state when a state-owned entity acts autonomously from the State. In order to establish that such entity acts autonomously, the Commission must examine various indicators. The indicators that the Commission must examine for determining the existence of State influence can be broadly divided into three categories: "organic and administrative links with the state, instructions issued by the state and the extent of supervision and scrutiny by the state".[9]

After examining the indicators falling under these three categories, the Commission could not find any evidence of Denmark and/or Sweden interfering in PNG's decision to grant a capital injection to PNL. With respect to the cross-subsidization complaint, the Commission explained that the complainant did

[9] State Aid SA.52489(2018/FC) – Denmark; State Aid SA.52658(2018/FC) – Sweden; Alleged State aid to PostNord Logistics: https://ec.europa.eu/competition/state_aid/cases1/202023/277215_2161570_141_2.pdf

not provide any information to sustain the allegations that Post Denmark cross-subsidized PNL's costs. The Commission also recalled that its own decision approving the compensation for the costs of Post Denmark's public service obligations included a mechanism for preventing overcompensation and that financial cross-subsidization would be possible only in the case of overcompensation. ITD has challenged this decision by the European Commission before the General Court of the European Union in case T-525/20 which is currently pending.

Another recent development concerns the ease of postal operators to get access to external funding, which is not State aid per se. In 2019, the Italian USP Poste Italiane obtained a €400 million loan from the European Investment Bank (EIB). The financing was specifically aimed at supporting and facilitating the deployment of Poste Italiane new strategic plan, called "Deliver 2022", throughout Italy..[10]The "Deliver 2022" strategy referred to the need to make the Italian postal operator a significant player in national, cross-border and international parcel delivery. Poste Italiane committed to use these resources to implement several projects, including the installation of energy-efficient solar panels in post offices and the improvement of energy-efficient standards across the postal network, the modernization of its logistics operations by increasing automated parcel sorting capacity, and the digitization of its operations. Overall, the number of postal operators trying to raise financing on competitive terms to support their growth plans is mounting in recent years.

4.2 The COVID-19 Crisis: Potential Spillovers for Postal Funding

Several discussions are taking place in the postal services market over the effects of the COVID-19 crisis. The implementation of restrictive measures, including lockdowns, have resulted in a significant increase in shipments of B2C parcel volume. The already growing e-commerce market has accelerated even more throughout 2020. However, the current crisis may also have long-term spillover effects which should be considered. In the next years, the EU will launch its NextGenerationEU plan to support Member States' recovery from the economic crisis due to the pandemic. The EU Recovery and Resilience Facility (RRF) will make €672.5 billion in loans and grants available to support investments undertaken by Member States. Traditional postal operators have an incentive to get access to these funds and use them not only to sustain their transformation into parcel delivery operators but also to fund their universal service obligations (USO).

Specifically, the EU RRF could become an appealing funding source for USPs given that almost 60% of the entire resources will be dedicated to support green

[10] Italy: Poste Italiane obtains EUR 400 m loan from EIB: https://www.eib.org/en/press/all/2019-249-poste-italiane-obtains-eur-400m-loan-from-the-eib

(37%) and digital (20%) investments.[11] Indeed, traditional postal operators' transition towards greener and more innovative technologies as well as their implementation of advanced digital shipping tools could be sustained by these forms of financing.

In addition, USPs will have most likely access to further resources via the European Green Deal Investment Plan (EGDIP). This is the investment pillar of the European Green Deal, whose main funding programs will mobilize €100 billion over the period 2021–2027 to boost sustainable investments in the EU. These resources will help the EU's transition towards a more energy-efficient economy by supporting the installation of networks of electrical vehicle charging stations as well as by funding installation of solar panels on public and private buildings, including warehouses and logistics facilities. It can therefore be expected that USPs will become increasingly active in seeking these funds.

5 Risk of Competitive Distortions

5.1 EU State Aid Rules Revisited

The mechanism so far used to fund the postal sector has been always aimed at compensating USPs for their USO-related burden. As a consequence, it is directly related to the net cost of universal service provision. Where EU Member States set up compensation funds to fund the USO, those needed to conform to the EU Postal Services Directive (Fratini, 2016). Financing of the postal sector through compensation funds has become now subject to EU State aid control and the compensation fund has been considered to constitute compatible aid. However, in recent rulings[12] the European Commission has shown awareness of the potential distortive effects of compensation fund mechanisms and has stated that any such mechanism should balance the goal of securing the USO with that of preserving fair competition in the market.

According to Article 107 of the TFEU, a measure constitutes State aid if four conditions are met: it is imputable to a Member State and granted through State resources, it gives a selective economic advantage to an undertaking, it distorts or threatens to distort competition, and it affects trade between Member States. It follows that compensation funds should be considered subject to State aid scrutiny, as clearly acknowledged by the Commission.

However, the alternative funding that USPs are now seeking to sustain their USO and support their transition to parcel delivery are not directly tied to the net cost of

[11] Recovery and Resilience Facility: https://ec.europa.eu/info/business-economy-euro/recovery-coronavirus/recovery-and-resilience-facility_en

[12] State Aid SA.35608 (2014/C) – Greece, Hellenic Post (ELTA) –Compensation for the financing of the universal postal service: https://ec.europa.eu/commission/presscorner/detail/en/IP_14_899

the USO. Most of these funds are instead only tied to innovation and transformation purposes. Moving forward, traditional postal operators might have an incentive in claiming that funds meant to support their transformation investments are instead essential to guarantee their USO because in that way the State support may easily be approved. Within an evolving postal services market, this new scenario could pose threats to fair competition.

As explained above, funds in the form of European loans or grants boosting the economic recovery of traditional postal services operators or financing their environmental and digital reconversion might provide undue advantages to those operators in the market. At the same time, these funds may also escape from State aid control. To better understand this, it is worth having a closer look at the EU State aid rules and principles.

Under EU State aid rules, public interventions in favor of companies are free of State aid when they are made on terms that a private operator would have accepted under market conditions. This principle is referred to as the Market Economy Operator Principle (MEOP). If this principle is violated, public interventions are considered State aid within the meaning of Article 107 of the TFEU, as they confer an economic advantage on beneficiaries that their competitors do not have. The Commission then proceeds to assess whether the aid can be found compatible with EU State aid rules. It follows that for funds such as European resources tied to economic recovery or transition, compliance with the MEOP may be more difficult to assess, leading to reduced scrutiny over the use of those same funds.

In the current COVID-19 crisis, Motta and Peitz (2020) argue that when aid is provided directly by national governments there is a high risk of a negative effect on the functioning of the Single Market. EU Member States hit by the pandemic have different fiscal positions, and there is a risk that in a given industry only some firms will receive support because only some Member States would be able to provide significant aid. This may create competitive distortions in the EU economy by altering the level-playing field within the Single Market. On the contrary, European funding programs based on common EU goals and harmonized approaches may entail lower risks of competitive distortions, by benefiting all companies operating in a specific industry and avoiding asymmetries in aid provision. Although these points seem valid, note that future EU funds like the Recovery and Resilience Facility (RRF) will be based on specific proposals made by EU Member States.

USPs in some EU countries have been already active in submitting to their respective governments project proposals to be financed by the upcoming EU recovery instruments. In September 2020, in an early version of a list of projects that was shared with the Italian government, Poste Italiane presented specific proposals to use €180 million from the RRF to fund investments for energy renovation of existing owned buildings, to install smart letter boxes and parcel lockers in rural areas far away from urban centers and to invest into proximity delivery points.

This example shows how USPs may leverage their positions as players who not only provide essential services but also own infrastructures that are essential assets for Member States' economic recovery. These arguments could be used to get access to additional European funds to finance both their strategic transformation and their USO with possibly minimal scrutiny exerted by EU and national regulators. Indeed, the main risk regards the opportunity for USPs to divert some of these transformation-dedicated funds towards funding the USO, in a potential attempt to circumvent State Aid Rules, therefore breaching the specific requirements of the EU Postal Services Directive.

5.2 How to Monitor Competition in a Rapidly Changing Market?

Concerns over risks for fair competition trigger some questions. What legal tools are currently in place to scrutinize alternative funding for postal operators, especially when funding is coming from European resources? And how can these tools help to avoid competitive distortions? To elaborate on these questions, we should take a look at the compatibility between State aid and EU funding.

A 2018 study requested by the European Parliament Budgetary Control Committee (CONT),[13] makes a clear distinction between two types of funds: EU funds that are channeled through managing authorities of Member States and EU funds that are granted directly to undertakings without coming under the control of a Member State's public authority. For the first type, EU funds become proper state resources and can represent State aid if all criteria of article 107 of the TFEU are met. For the second type, EU funds cannot be considered as state resources and therefore do not constitute State aid.

The above distinction is very important. One necessary criterion for public aid to be considered State aid is the actual transfer of resources controlled by the state. Control of resources by the state also implies that the state has some level of discretion to determine the beneficiaries of a public aid and make resources available to them. That is why EU funds channeled through Member State's authorities can represent State aid. A clear example is represented by European Structural Funds (ESF), which are managed by Member States. Another example will be the EU Recovery and Resilience Facility (RRF), as Member States will be able to channel those funds to specific sectors and undertakings according to their own economic priorities. When instead EU funds are directly assigned to local undertakings, there is no transfer of state controlled resources and, in principle, no need for State aid scrutiny. This is the case of funds granted as loans to Member States' major economic players by the European Investment Bank (EIB) as they do not represent State aid.

As explained earlier, in the postal services market USPs are seeking additional funding through several EU financing instruments. These instruments include both

[13] "State Aid and EU funding: Are they compatible?", Analysis requested by the Budgetary Control Committee: https://www.europarl.europa.eu/cmsdata/142819/Briefing_State%20Aid%20and%20EU%20funding_Final.pdf

funds that can be channeled through Member States' authorities and funds that can be directly assigned by the EU to national undertakings. It turns out that the financing mix may increase the legal complexity of assessing potential competitive market distortions, as the impact of some funds may be subject to specific State aid scrutiny while the impact of other funds may not.

In the midst of the COVID-19 crisis, the European Commission has also adopted a State aid Temporary Framework to enable Member States to financially support their economies by using all the flexibility foreseen under State aid rules. This was meant to guarantee sufficient liquidity to Member States' businesses during the crisis and allow continuity of economic activities. At the same time, the Commission is conducting a review of the General Block Exemption Regulation (GBER) aimed at exempting from prior Commission scrutiny those aids granted through national funds for projects supported under certain EU funding programs.

However, for the postal services market such a scenario raises concern for the future monitoring of competition. The combination of increased temporary flexibility in granting financial support to national incumbents and the relaxation of ex ante scrutiny requirements for EU funds channeled through Member States' public authorities may weaken the existing toolbox being used to avoid competitive distortions and result in undue advantages for USPs.

To balance this greater flexibility given to Member States the Commission seems oriented to require Member States to carry out more ex post assessments on aids' anticompetitive effects, but this mechanism may be difficult to enforce and have limited effectiveness, as it is unclear what could be the consequences once anticompetitive effects are identified.

5.3 Remedies Recommendations

In an evolving postal services market, the issues of USO definition and USO compensation remain very challenging and are becoming even more complex. The ability to compensate the USP for the net cost burden of the USO should remain in place, but if this does not come directly from national governments, resorting to other forms of compensation may entail anticompetitive effects. As described, the risk of competitive distortion can be high in case of the introduction of a compensation fund to be paid by other postal market operators.

The fact that EU State aid rules would apply to compensation funds may provide a guarantee against serious market distortions. The risk of anticompetitive effects, however, is even greater when looking at the many alternative sources of funding that USPs are now exploring. Indeed, USPs may seek these funds to finance their on-going transformation and then divert them to also cover their USO costs, and as these resources include especially a wide range of EU funds the applicability of State aid scrutiny to them cannot always be guaranteed.

The Free & Fair Post Initiative (FFPI) has proposed recommendations to remedy potential competitive distortions. One proposal is that funding mechanisms aimed to assist the modernization of USPs as state-owned incumbents should be offset by providing proportional incentives to other postal market operators to ensure a level playing field. This could be applied in cases of both direct governmental funding and indirect funding when EU funds are channeled through Member States' authorities.

Another way to remedy potential competition distortions would be to include further provisions to promote competition within the EU Postal Services Directive (PSD). As a consultation process on the need to revise the current PSD is now undergoing, it could be useful to provide additional guidance on the provisions to adequately promote competition in the margins of the PSD review. This could be done in the form of an update of the 1998 Notice on the application of competition rules to the postal sector.[14] For instance, this update could introduce limitations to the options of Member States who may wish to privilege state-owned incumbents, either directly or indirectly.

However, these proposed remedies are not sufficient. Given the variety of funds potentially available to traditional postal operators, a comprehensive scrutiny of these funds and their effects remains very challenging. With respect to EU funds, as the Commission aims to improve the interplay between EU funding rules and EU State aid rules by relaxing ex ante scrutiny requirements, it may still be important to retain some sort of ex ante control on funds allocation. For instance, this could occur via ex ante impact assessment analysis in order to avoid relying only on the ex post observation of effects on competition.

6 Conclusions

This paper has outlined the significant transformation of the postal services market during the last decade, marked by continuous letter mail decline and increased delivery of parcel volume. These two trends are challenging traditional postal operators' abilities to meet and sustain their USO, while driving changes in operations, costs' structures and consumers' behaviors. USPs are trying to adapt by investing in new infrastructure and technology to support the delivery of parcel volume whilst coping with the obligations related to declining letter mail volumes.

In order to fund these investments, traditional postal operators can no longer rely only on compensation for the cost of universal service provision, as defined in the PSD, and are now turning to alternative funding. These new forms of financing can include ownership restructuring operations as well as access to grants and loans from national funds and EU funding programs. In particular, as a response to the current COVID-19 crisis, many additional EU resources should soon become available. This financing mix may increase the complexity of assessing potential

[14] Notice from the Commission on the application of the competition rules to the postal sector and on the assessment of certain State measures relating to postal services - (98/C 39/02).

competitive market distortions, as the impact of some funds may be subject to specific State aid scrutiny while the impact of other funds may not. USPs may have incentives to divert some of these transformation-dedicated funds towards funding the USO, in a potential attempt to circumvent State aid rules.

When focusing on EU funds, relaxation of ex ante scrutiny requirements for EU funds channeled through Member States' authorities can seriously weaken the existing toolbox being used to avoid market distortions and result in undue advantages for USPs. Proposals to avoid or remedy distortions include the provision of economic compensations to other postal operators in case of relevant state funding addressed to support USPs' modernization and also the promotion of market competition by including in the EU PSD restrictions to Member States' ability to financially support state-owned postal incumbents. However, performing a comprehensive State aid scrutiny for all available funds and their individual as well as combined effects remains a complex exercise, and it will be important to still retain ex ante control on the distribution of funds.

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