

Australia Post

DETERMINING LEVELS OF COMPENSATION FOR LOSS OR DAMAGE OF POSTAL ITEMS

February 2010

Report by the Commonwealth and Postal Industry Ombudsman,
Prof. John McMillan, under the *Ombudsman Act 1976*

REPORT NO. **01|2010**

Reports by the Ombudsman

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EXECUTIVE SUMMARY

Compensation may be payable by Australia Post if postal items are lost or damaged. For items other than those sent by registered post or cash on delivery, the maximum compensation payable under Australia Post's terms and conditions is \$50.

If an item is sent registered post or cash on delivery, a maximum basic compensation level of \$100 is applicable. 'Extra Cover' (formerly called insurance) up to \$5,000 can also be purchased for these items.

In our view, some form of compensation is a necessary feature of the postal service. People have a right to expect some level of recompense if their property is lost or damaged while in Australia Post's hands. The liability to compensate for service failure also acts as an incentive to optimise service delivery.

It is reasonable for Australia Post to limit its liability for loss and damage in the post. Australia Post has no way of knowing the value of items that people may be sending. Loss and damage may not be Australia Post's fault. Limitation of liability is common in the postal and courier industry.

However, Ombudsman office records show that there was a maximum compensation level of \$50 payable as long ago as 1987. Changes in the value of money brought about by inflation since 1987 mean that \$50 now is worth only half what it was worth then. Without expressing a particular view about the level of compensation, we note that if the amount had been increased in line with the consumer price index, the 2009 figure would be \$100.60.

As the level of standard compensation is a regular issue of complaint to our office, we decided to investigate why the compensation level has remained unchanged for so long. We do not claim to have the expertise to indicate an appropriate level of compensation. We do, however, consider it appropriate to investigate the process used by Australia Post to determine compensation levels given the substantial erosion in the value of the maximum payable.

In response to our enquiries, Australia Post advised us that there had been changes to compensation levels since 1987. In 1989, an enhanced maximum compensation level of \$75 was made available for items sent by certified mail. In 1996, when the certified and security mail services were replaced by the new registered post service, a basic compensation level for that service of \$100 was introduced, and the rate for ordinary postal items was confirmed at \$50.

Australia Post considers that \$100 was and remains an attractive basic compensation level for registered post, taking pricing and marketing considerations into account. It considers that the compensation level for ordinary items should be differentiated from registered post, effectively by being kept at half the level applicable to registered items.

In our view, this forges an unwarranted and misleading link between the terms and conditions on which Australia Post offers its registered service, in relation to which it competes with other couriers and postal operators, and the terms and conditions on which Australia Post's monopoly letters service is provided.

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In addition, there was presumably a rationale for the figure of \$50 being in place in 1987. This may have been based on considerations such as the type and value of items deemed by Australia Post as suitable for the ordinary (as opposed to registered) post, community standards regarding items deemed suitable for the ordinary post, and the cost to Australia Post of providing compensation at that rate.

Given that the real value of compensation for ordinary items today is only half what it was in 1987, the rationale applicable in 1987 no longer seems to be relevant or applied by Australia Post. We do not know whether Australia Post has carried out any analysis to justify the declining real value of compensation for ordinary items. The information it provided to us suggests that the compensation level for ordinary items is set solely by reference to the level for registered items.

We note the tendency for the diminishing level of compensation for ordinary post to dissuade people from using the ordinary letters and parcels services in favour of registering items, in order to secure adequate cover should their postal items be damaged or lost.

We consider that the compensation level payable for service failure in relation to the monopoly letters service is closely bound up with issues around the pricing of that service. The Australian Competition and Consumer Commission (ACCC) has statutory powers to enquire into, and report upon, proposed price increases for the letters service. In our view, the question of compensation payable for service failures is a relevant consideration in the exercise of those powers.

In relation to Australia Post's other services to which the basic compensation level applies—most notably parcels—we consider that the steadily declining real compensation rate is worthy of note and will tend to steer customers towards the more expensive registered service.

This has implications particularly for residents of regional and rural Australia, who have only limited access to competitors' services. If this is deliberate Australia Post policy, then it may be a matter worthy of public debate.

On the basis of this investigation, the Ombudsman recommends that Australia Post should as soon as practicable conduct a formal review of the amount of compensation it pays for loss of, and damage to, ordinary items. We also propose that compensation rates should be part of the ACCC's consideration of proposals to increase the basic postage rate, and that Australia Post should incorporate information about its compensation arrangements and how they have changed over the relevant period in any future price notification to the ACCC.

We will follow up with Australia Post in six months in relation to its implementation of these recommendations. We will also provide a copy of this report to the ACCC.

PART 1—BACKGROUND

Payment of compensation by Australia Post

1.1 Of the millions of postal items handled by Australia Post every day, the vast majority reach their destination safely. However, inevitably some items are lost and damaged while in transit.

1.2 This is not necessarily the result of any fault on the part of Australia Post or its employees. Through our investigation of complaints we have encountered many different causes of loss and damage, ranging from arson of street posting boxes, to transport accidents. Equally, however, loss or damage may be caused by lack of care and skill in handling, or even outright dishonesty and theft, by mail handlers.

1.3 There are limitations on Australia Post's legal liability for items lost and damaged in the mail. Chief of these is the provision in the *Australian Postal Corporation Act 1989* (the APC Act) that Australia Post is not liable for loss or damage caused by any act or omission in relation to the carriage of a letter or article, unless Australia Post has given the claimant a receipt for the article.

1.4 The APC Act also provides that unless a customer enters into a different agreement with Australia Post, the terms and conditions under which articles are carried are those made by the Board of Australia Post.

1.5 The Board has made terms and conditions that seek to exclude any liability for loss of, and damage to, postal items, or for misinformation by Australia Post employees. The terms and conditions nevertheless provide for compensation to be paid in some circumstances.

1.6 Where an item is sent by registered post or cash on delivery (COD), compensation for loss or damage may be payable in accordance with the Extra Cover terms and conditions. This is up to a basic maximum of \$100 for registered items or up to \$5,000 if the customer purchases additional Extra Cover.

1.7 In addition, the terms and conditions provide that Australia Post can pay up to \$50 compensation at its discretion for loss of, and damage to, ordinary postal items.¹ There are limitations and exclusions on when compensation may be paid.

1.8 The net effect of the terms and conditions is that, generally speaking, unless a customer uses registered post or COD, a maximum of \$50 compensation for loss and damage is payable.

1.9 This report does not consider the legal validity of the terms and conditions, or their consistency with other legislation. For present purposes it is assumed that the limitations and exclusions of liability contained in the terms and conditions are legally effective and would be upheld if tested in a court of law.

Our investigation

1.10 In the financial year ended June 2009, 470 out of 2,219 complaints made to the Postal Industry Ombudsman about Australia Post concerned loss of a postal

¹ An 'ordinary' item is one that has not been sent by the registered post or COD service.

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item. This represents 21.2% of the Australia Post complaints we received. Many of these complaints raised issues about the payment or amount of compensation.

1.11 We are aware that complaints about loss are a significant issue for Australia Post. In written replies to the Senate Standing Committee on the Environment, Communications and the Arts Budget Estimates hearings in May 2008, Australia Post advised that in 2007 its centralised enquiry number received 224,000 complaints that involved searching for a missing item.

1.12 Complainants often say to us that they have been offered the maximum compensation of \$50 for ordinary articles, but that this amount would not fully compensate them for their loss.

1.13 Our usual response to complaints of this nature is that customers may register their items or purchase Extra Cover for them. While this option is not available for Express Post items, customers do have a choice between Express and Registered Post. By selecting Express Post, customers choose not to obtain the benefit of Extra Cover.

1.14 For this reason, we do not generally investigate complaints about claims that the compensation for ordinary items is inadequate to cover the customer's loss. We do so only where a serious and identifiable service failure by Australia Post caused the loss—one which went beyond the general risk of loss and damage it must be assumed customers accept when they consign items by post.

1.15 We are aware, however, that the maximum rate of compensation for lost ordinary items has not changed for many years. This was highlighted when a review of old files held by the Ombudsman showed references to a compensation rate of \$50 as long ago as 1987.

1.16 Since 1987, the cost of postage has increased materially. For example, the basic letter service—that is, the letter service that Australia Post is required by law to provide across Australia at a flat rate of postage—has increased in price from 37¢ to 55¢ since 1987.

1.17 We decided to contact Australia Post to seek information about the history of compensation rates since 1987, and the basis on which the rates were set.

Australia Post's response

1.18 We provided a draft version of this report to Australia Post for comment. Its response is reproduced in full at appendix 1 of this report.

1.19 Australia Post has rejected the thrust of this report and the recommendations in it. Australia Post maintains the view that the level of compensation for ordinary mail should be tied to the basic level of compensation for registered post, which for commercial reasons it considers should be \$100.

1.20 Australia Post has also indicated that its view is that compensation levels are not relevant to the pricing of the basic letter service, having in mind the low level of compensation payments made for failures of that service.

1.21 The Ombudsman believes it is time to thoroughly review compensation levels. Australia Post's reasons for disagreeing with the Ombudsman do not address the

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major issue, which is that the same compensation level has been in place for 22 years, and should be revisited.

1.22 As to the pricing of the basic letter service, Australia Post's view that there is no connection between compensation levels and the price of the reserved postal service requires further analysis and justification. Accordingly, this report recommends that information about compensation arrangements, including when they were last changed and what proposals exist to review them, be provided in any future price notification by Australia Post to the ACCC.

PART 2—ISSUES

Why pay compensation?

2.1 For most businesses, liability to compensate dissatisfied customers will be fixed by contract. In many jurisdictions, the law implies some basic contractual terms about providing services with reasonable care and skill, which could lead to compensation being payable if breached. Businesses may also be liable to pay compensation for negligence if that negligence causes loss of, or damage to, other people's property.

2.2 As well as legal liability of this sort, businesses may choose to pay compensation despite not being legally liable to do so, in order to retain customer loyalty. In such circumstances, businesses are likely to be concerned with making the level of compensation attractive to customers.

2.3 Australia Post is in a somewhat different position in that its terms and conditions are not governed by the law of contract. Instead, they have effect because the APC Act says that they do. Accordingly, the Australia Post Board has a measure of flexibility in making terms and conditions independent of market forces and the general law of contract.

2.4 In structuring its pricing arrangements to be both competitive and profitable, a business will need to consider the frequency with which it is likely to have to compensate customers and the amount it is likely to have to pay. In a competitive environment, a business must provide a level of compensation that compares favourably with its rivals, or risk losing business to them.

2.5 Another consideration for business is, of course, minimising the number of occasions on which it has to compensate dissatisfied clients. Strong quality assurance mechanisms will necessarily reduce a business's exposure to compensation payments.

2.6 In our view, these principles apply equally to Australia Post, with one notable difference. In respect of the basic letter service, Australia Post is not subject to competition because it has a statutory monopoly on the collection and delivery of letters under 250 grams and 5 mm thick² (known as the 'reserved services').

2.7 Australia Post therefore lacks the same incentive to provide compensation for failures in the reserved services as would exist in a competitive environment, because customers do not have the choice to take their business elsewhere if they are dissatisfied with the compensation payable.

Compensation as 'sound commercial practice'

2.8 Australia Post is under a legal obligation to act in accordance with sound commercial practice. This may imply that Australia Post should always seek to maximise its profits and take advantage of its monopoly position in relation to reserved services.

2.9 An alternative interpretation, at least in respect of the reserved services, is that Australia Post should act as though it is subject to market forces—even though it

² Subject to certain exceptions spelt out in the APC Act, Australia Post effectively has both an obligation to provide, and a monopoly over, the basic letter service in Australia.

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is not. In relation to compensation, this would involve setting compensation at a level that is equitable for Australia Post's customers, having in mind the cost of the service provided and the reasonable expectation of customers that appropriate care will be taken in the handling of their mail.

2.10 There is another way in which liability to pay compensation promotes sound commercial practice, and that is by providing an incentive to improve service and product quality. If compensation has to be paid for service failure, whether because of legal liability imposed from outside or commercial imperatives to keep customers happy, there is a cost incentive to minimise compensation payouts by optimising service delivery.

2.11 It may therefore be a further aspect of operating in accordance with sound commercial practice that Australia Post recognises an obligation to compensate for service failure and sets the amount of compensation at a realistic level. By allocating compensation payments to the responsible cost centres, an incentive is provided for service improvement and higher visibility of problems is achieved.

2.12 It is not in our view unreasonable for Australia Post to limit the extent of its legal liability to customers through its terms and conditions. We often have to remind complainants that Australia Post may have no way of knowing what has been posted in a parcel or its value.

2.13 Private businesses often limit their liability by use of contractual terms, subject to rules of law governing when terms of this nature can be said to have been effectively incorporated in a contract and subject also to laws about unfair contract terms and trade practices.

2.14 It would not be fair in those circumstances to expect Australia Post to pay unlimited compensation for loss, even where the loss is caused through its fault, noting that the loss may not be Australia Post's fault at all.

2.15 However, we do consider that it is appropriate for Australia Post to have some form of compensation scheme. In our view, the provision of basic compensation is an aspect both of Australia Post's obligation to provide a letter service to all Australians, and its obligation to act in accordance with sound commercial practice. It is questionable whether provision of a service that did not provide some sort of compensation, albeit subject to conditions, for service failure would meet those obligations.

How much compensation?

2.16 It is not the Ombudsman's function to set the amount of compensation that should be payable by Australia Post for service failure. The Ombudsman's office does not have the mandate or expertise to conduct the analysis that would be required to strike the balance between profit, equity to customers, and the quality control incentive referred to previously.

2.17 This report examines why the level of compensation for loss of, or damage to, ordinary items that is payable by Australia Post in 2009 is the same as the level prevailing in 1987.

The changing value of money

2.18 When comparing historical levels of compensation with the present day, it can be useful to consider how the value of money has changed over time. Ombudsman files indicate that a maximum of \$50 compensation for loss and damage was paid by Australia Post as long ago as 1987. In real terms, \$50 in 1987 was worth more than it is today.

2.19 People are, generally, familiar with the concept of the changing value of money. In brief, the result of inflation is that a dollar will not buy as much today as it did 20 years ago. One way of measuring this is the Consumer Price Index (CPI), which tracks how much a set selection of goods costs over time, and uses changes in the cost of the goods to measure changes in the value of money.

2.20 Measured by the CPI, the value of money has halved in the past 20 years.³ That is, in 2009 the same selection of goods would cost double what it did in 1987. On that basis, \$100 at 30 June 2009 is equivalent to \$49.70 in 1987.

2.21 Not all goods change in value at the same rate. Appliances such as televisions and other electrical goods may decrease in price over time, whereas other goods have increased in price more than the CPI would suggest. This is because the CPI averages out price increases across a range of goods.

2.22 Of particular relevance to the question of compensation for postal services is the change in the price of those services over time. A good benchmark is the basic postage rate, or the price of a standard postage stamp.

2.23 In 1987, the basic postage rate was 37¢, compared to 55¢ today. Last year, Australia Post notified the ACCC of its proposal to increase the amount to 60¢, although the proposal did not find favour with the ACCC.

2.24 The cost of postage has not risen as fast as the CPI; since 1987 the CPI has doubled but the price of a stamp has not. The 55¢ cost of a basic postage stamp today is 27¢ in 1987 terms, compared with the actual cost of a stamp in 1987 of 37¢. Nevertheless, the price of postage has risen, just not as fast as other goods and services.

2.25 In our view, this raises two considerations:

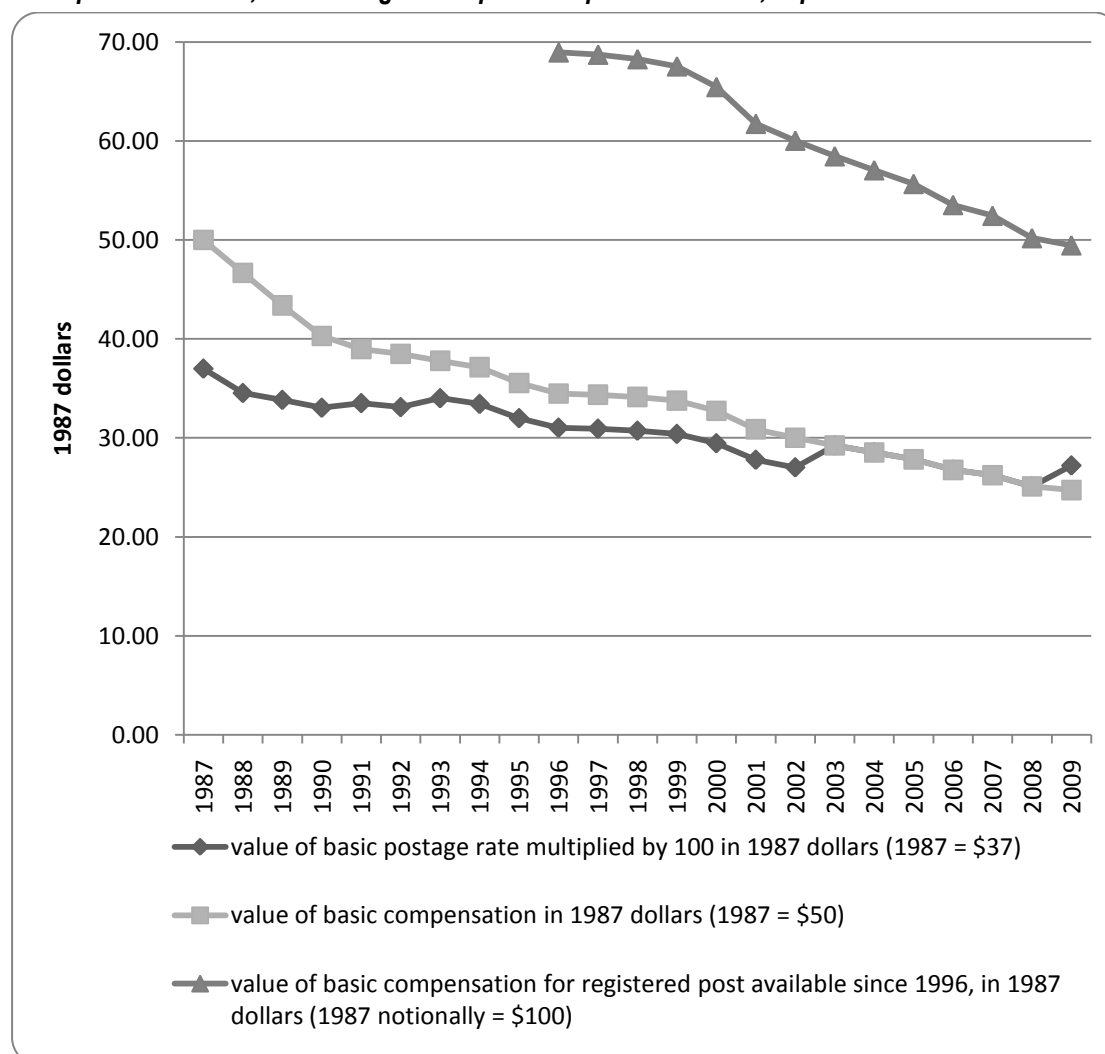
- Why did Australia Post consider \$50 an appropriate amount of compensation in 1987 (or at the date that this figure was set, if earlier)? Was this amount related to the value of articles that Australia Post expected people to send through the post without purchasing additional insurance? Was there any other rationale for the figure?
- Has Australia Post considered reviewing the \$50 compensation maximum? In 1987 dollars, \$50 today is only worth \$24.85. If there was a rationale for the figure of \$50 in 1987, does it still apply?

As part of our investigation, we asked for Australia Post's comment on these questions.

³ Figures from the Australian Bureau of Statistics website www.abs.gov.au.

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Table 1: Comparisons of changes over time in the value of the basic postage rate, the basic compensation level, and the registered post compensation level, expressed in 1987 dollars



Australia Post's position

2.26 In response to our initial investigation, Australia Post provided us with information about the levels of compensation it had set and how these had changed over time.

2.27 Australia Post agreed that the maximum level of compensation for ordinary items had been \$50 in 1987, but said that in 1989 this was increased to \$75. The level was reconsidered when Australia Post reviewed its certified and security mail services in the mid-1990s and replaced these with the new registered post service in 1996.

2.28 When the new registered post service was introduced, Australia Post decided to offer a base level of \$100 compensation for loss of, and damage to, registered post items. Additional cover could be purchased up to the current maximum of \$5,000. Australia Post advised that the base level of \$100 was considered to be:

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... the most appropriate and effective compensation point, from both a market positioning and service cost perspective.⁴

2.29 No doubt \$100 was seen in 1996 to be marketable as an improvement on the \$75 cover for certified and security mail. It is perhaps worth noting that in 1989–90, when the \$75 limit was introduced, \$75 was worth \$60.75 in 1987 dollars. When the figure of \$100 for the new registered post was introduced in 1996, it was worth \$68 in 1987 dollars and the value of \$75 had fallen to \$51 in 1987 dollars.

2.30 Australia Post advised us that the return to a \$50 maximum for ordinary items in 1996 intended to provide a clear product/service differentiation between ordinary and registered post. We understand that Australia Post considered it appropriate to provide maximum compensation for ordinary items at half the base rate available for registered items.

2.31 Australia Post has told us that while it had increased the price of registered post over time, it still considered the base level of \$100 compensation cost effective and beneficial, from a marketing perspective. It has no plans to increase the \$100 figure and, because the rate of compensation for ordinary items is linked to the rate for registered post, there are no plans to increase the figure for ordinary items either.

Distinctions between registered post and ordinary post

2.32 Australia Post is required by law to provide the reserved services. Other operators are barred from offering them, unless they charge at least four times what Australia Post charges. In contrast, Australia Post is under no obligation to provide a registered post service and other operators may provide a similar service in competition with Australia Post if they wish.

2.33 Australia Post offers the registered post service (and, it should be noted at this point, its parcels service) as part of its principal function under the APC Act to provide postal services. It does so in competition with other companies that collect and deliver courier items and parcels.

2.34 The price of the non-reserved services is a matter for Australia Post to decide, based on normal considerations of market pricing. In contrast:

In order to increase the prices of its reserved letter services in accordance with the *Trade Practices Act 1974* (the TPA), Australia Post must provide the ACCC with a locality notice specifying the proposed price increases, and receive a response from the ACCC stating that it has no objection to the proposed price increases, or price increases that are less than those proposed by Australia Post.⁵

The Minister has the right of veto over any proposed price increase for the reserved services.

2.35 If customers find the \$100 basic level of maximum compensation for registered post unacceptable, they have two options—they can use the services of a competitor or they can choose to purchase Extra Cover for the item.

2.36 Customers do not necessarily have these options for ordinary items if they are dissatisfied with the \$50 maximum compensation. For the reserved services, Australia Post has no competitors because competition is outlawed. For ordinary

⁴ Australia Post response to our investigation, 18 June 2009.

⁵ ACCC issues paper on Australia Post's draft price notification, August 2009.

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parcels, customers can take their business elsewhere. However, in many rural and regional areas this is not a practical solution because there is no accessible competitor. Extra Cover is not available unless an item is registered.

2.37 Australia Post's argument that \$100 is a good basic compensation level from a marketing and cost point of view is not in itself unreasonable. That said, it should be observed that the real value of \$100 has diminished over time. Between June 1996 and June 2009, the CPI has increased by 39%. In other words, \$100 in 1996 is worth only \$71.75 today.

2.38 By not increasing the basic level of compensation, Australia Post is shifting customers not satisfied with this level of cover towards purchasing Extra Cover as an 'add-on'.

2.39 In contrast, customers requiring more than the \$50 maximum compensation on ordinary items can only increase their cover by registering the item. A customer intending to use the reserved letter service to send an item cannot do so if they want more than \$50 cover—instead, they must use the non-reserved registered service.

2.40 In our view, Australia Post's suggestion that the compensation provided for the reserved services should be set as a proportion of the cover provided for the non-reserved registered service makes an unwarranted link between the terms and conditions on which the reserved services are supplied, and the terms and conditions of a non-reserved service (registered post).

2.41 Although the argument does not apply in the same terms to the ordinary parcels service (as it is not a reserved service), we consider that there is nonetheless a debate to be had about the way in which risk is shared between Australia Post and its customers in the event of loss of, or damage to, postal items.

2.42 Particularly for Australians living in rural and regional areas, Australia Post may be the only realistic choice when sending parcels. The diminution in the real value of compensation for loss of, or damage to, ordinary parcels raises questions about the reasons for shifting risk of service failure from Australia Post to the consumer, and whether this is a deliberate policy or an unintended consequence of long-standing inaction.

The rationale for \$50

2.43 Australia Post advised us that the figure of \$50 for compensation for ordinary mail was set in 1996, having regard to the \$100 figure for registered mail. The \$100 figure was arrived at by a process of deciding what was cost-effective and 'saleable' and, we infer, as an increment from the existing \$75 for security and certified mail.

2.44 This does not explain how the figure of \$50 current in 1987 was determined. Nor does it reveal the process by which earlier figures were reviewed and increased if necessary.

2.45 We assume that, periodically, Australia Post must have reviewed the 'basic' compensation to be paid for loss of, and damage to, items sent using the reserved services. As previously stated, we consider that a compensation scheme is a necessary part of the provision of the reserved services. As long ago as 1987, Australia Post considered \$50 an appropriate sum of compensation.

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2.46 In our view, Australia Post has not satisfactorily explained why the maximum compensation payable for ordinary and reserved services items has halved in real terms since 1987.

2.47 Even if it is accepted that the introduction of the registered service in 1996 provided a basis for 'resetting' the basic figure to \$50, that sum today is worth \$35.90 in 1996 dollars.

2.48 The devaluing over time of the compensation payable for ordinary mail, including the reserved services, might have influenced customers who would previously have been content to use the reserved letter service to instead use the non-reserved registered service.

The need for review

2.49 In our view, the provision of some level of compensation for service failure is an integral part of the reserved letter service. There is no doubt an expectation on the part of customers of other ordinary mail services that they will be compensated in the event of loss of, or damage to, their mail.

2.50 It seems to us that the maximum amount of compensation payable, particularly for the reserved services, should not be a random choice. Rather, it should be based on some level of analysis of:

- the type and value of items people send and for which they seek compensation
- community standards in relation to 'valuable' items that should be sent by a more secure service, such as registered post
- the cost to Australia Post of providing compensation at a given rate for ordinary items, and its effect on the pricing of the ordinary services, including the reserved letter service.

2.51 If an analysis of this sort was carried out in 1996 when the figure of \$50 was set, then by reason of the changing value of money and price of postage, it may no longer be valid and should be updated.

The level of compensation and the cost of postage

2.52 At a broader level, we consider that there would be an expectation among mail users that the level of compensation for service failure should keep pace in some way with the changing value of money, and should at least be reviewed whenever the cost of basic postage is reviewed.

2.53 Australia Post must provide notification to the ACCC of any proposed price increase for its reserved services. The ACCC has a role in considering and reporting on such proposals.

2.54 In considering these notifications, the ACCC gives regard to various factors, including:

... the need to discourage a person who is in a position to substantially influence a market for goods or services from taking advantage of that power in setting prices⁶

⁶ *Trade Practices Act 1974 s 95G(7)(b).*

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and

the functions and obligations of Australia Post as set out in sections 14–16 and 25–28 of the *Australian Postal Corporation Act 1989*.⁷

2.55 One of the obligations is to provide the reserved services. One of the functions—indeed, the principal function—is to supply postal services within Australia.

2.56 We argue that the availability of appropriate compensation for service failure is an integral part of the provision of the reserved services and of postal services generally. In our view, the adequacy of the compensation provided—which should encompass a consideration of whether the level of compensation has been reviewed appropriately having regard to the changing value of money—is a factor to which the ACCC could have regard in considering any notification of a proposal to increase the basic postage rate given to it by Australia Post.

2.57 This is the more so because, as we discussed earlier in this report, the setting of compensation levels is closely bound with the pricing of a product. The optimum compensation level will depend on a number of factors, including the price of the service involved; and conversely that the price of the product may be affected if the level of compensation for service failure changes.

⁷ Direction made by the Minister under his statutory powers on 19 September 1990.

PART 3—CONCLUSIONS

3.1 We consider there are two broad areas Australia Post should address.

3.2 First, we do not accept that there should be a link between the level of compensation paid in respect of service failure in the reserved services and the level payable for service failure for the non-reserved services. Different considerations apply to the two. While Australia Post can argue that the pricing and compensation provisions for non-reserved services are matters of commercial judgement, the same does not apply to the reserved services. One should not depend upon the other.

3.3 By setting the compensation level at a specific figure for reserved services and then letting that level be eroded by inflation over time, customers are likely to be influenced away from using the reserved services because the maximum level of compensation is inadequate.

3.4 The rationale for the basic level of compensation for the reserved and ordinary parcels services should depend on more than Australia Post's judgement about the commercially attractive level for registered post and its decision to maintain differential pricing between the two.

3.5 Australia Post should appreciate that because it has failed to change the basic level of compensation over time, people can no longer send by ordinary mail items that they could have sent 10 or 20 years ago and expect to be fully compensated if the items are lost or damaged.

3.6 The implications of the erosion in the value of the basic compensation for users of ordinary mail services are clear. Any influence on people to substitute use of the non-reserved registered service where they would previously have used the reserved letter service may raise questions about Australia Post's commitment to maintaining the standards of the basic letter service.

3.7 In relation to the non-reserved parcels service, if Australia Post hopes to persuade people to purchase registered post and Extra Cover for their mail items in order to receive adequate compensation in case of service failure, we consider that Australia Post should be transparent about this approach. It should be prepared to debate the merits of the effect this will have on users, particularly users in rural and regional areas who have limited access to competitors' services.

3.8 Second, we have noted the apparent lack of any review of compensation levels when the basic price of postage has been increased.

3.9 We have already clarified that we do not consider that our role, or the scope of this report, extends to any discussion of what would constitute an appropriate compensation level. However, we are of the view that the ACCC has the appropriate expertise and the legal authority to express a view on the subject in relation to price notifications by Australia Post.

3.10 Accordingly, we consider that the compensation provisions applicable to the reserved services are relevant to any price notification submitted by Australia Post to the ACCC. We take the view that Australia Post should include some discussion of those provisions in any price notification, and, whether or not it does so, the ACCC could usefully inform itself of such provisions and take them into account when considering a price notification by Australia Post.

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3.11 Australia Post could also address the issues discussed in this report by creating a link between the cost of postage and the compensation available for service failure. In other jurisdictions the link is specific. For example, in the UK the compensation available for loss of, or damage to, ordinary mail is capped at 100 times the cost of a first class stamp.⁸

3.12 Whether Australia Post chooses a strategy of that kind, or a different way of reviewing and keeping current the basic level of compensation it pays, it needs to establish a strategy for handling this issue in the future. We do not consider that inaction over a period of 13 years is acceptable.

⁸ Royal Mail's retail compensation policy for loss, <http://www.royalmail.com/portal/rm/content2?catId=70700722&mediaId=79800735> and Royal Mail's compensation policy for damage, <http://www.royalmail.com/portal/rm/content2?catId=77300736&mediaId=80000739>, last accessed on 19 January 2010.

PART 4—RECOMMENDATIONS

4.1 I make the following recommendations:

Recommendation 1

Australia Post should as soon as practicable conduct a formal review of the amount of compensation it pays for loss of, and damage to, ordinary post items. The review should address, at least, the following:

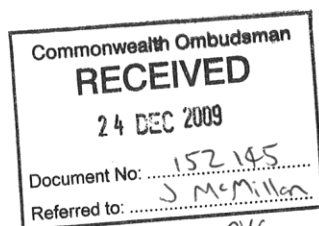
- identification of the rationale for the figure being set at \$50 in 1987
- whether that rationale is still valid independent of the compensation levels payable for other services, and if not, why not
- identification, if that rationale is still valid, of the compensation level that would be required to fulfil the same purpose at 2010 values.

Recommendation 2

Australia Post should incorporate information about its compensation arrangements and how they have changed over the relevant period in any future price notification to the ACCC relating to a proposed increase in the basic postage rate.

4.2 We will follow up with Australia Post in six months in relation to its implementation of these recommendations. We will also send a copy of this report to the ACCC.

APPENDIX 1—AUSTRALIA POST'S RESPONSE



CORPORATE SECRETARY

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22 December 2009

Professor John McMillan
Postal Industry Ombudsman
GPO Box 442
CANBERRA ACT 2601

Dear Professor McMillan

Thank you for the opportunity to provide our comments on the contents of your draft report titled "Determining Levels of Compensation for Loss or Damage of Postal Items".

As a general observation the content of this report focuses on the amount of compensation available for those items carried via the letter service which encompasses small (standard) and large letters and therefore is a mix of reserved and non-reserved services.

Although Section 27 of the Australia Post Corporation Act (the Act) requires the Corporation to offer a letter service, it is not restricted to just reserved letters and it does not include any obligation to provide compensation for either reserved or non-reserved items. Furthermore Section 34 of the Act provides immunity from liability for lost or damaged items where the item has been sent using the letter service except where a receipt has been issued.

In this context it should be noted that the current compensation limit for ordinary mail items have been designed primarily for articles of value which are overwhelmingly sent by the parcel service, which is not a reserved service.

This view is supported by the 2008/09 statistics which show that out of a total volume of 43.8 million ordinary parcels mailed, 9,124 or 0.02% made compensation claims; with an average payout value of \$38.03. These claims represent just under 72% of the total number of compensation claims for ordinary mail items received during 2008/09.

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In contrast, out of the 4,259.1 million items posted in the domestic letters service, 666 compensation claims were received. This figure of 666 represents less than one in six million letters and is only 5.2% of the total compensation claims for mail items with the average amount paid being \$28.83.

As advised previously, we do not consider that there is a relationship between compensation limits and the basic postage rate. Any refund on postage is treated as a separate amount to any compensation claim. Furthermore, the cost of providing the letter service is a factor that is taken into consideration in setting letter prices. However, as noted above the amount of compensation paid is a minimal cost in Australia Post providing the letter service.

However, given the nexus between the ordinary mail and basic Registered Post compensation levels, any change to the former will ultimately be dependent on an adjustment to the latter. In this regard the base Registered Post level of cover is still considered the most appropriate and effective compensation point from both a commercial and service cost perspective. Although there are no immediate plans to adjust this level, it will be kept under review as part of our ongoing product/service monitoring.

In regard to our latest draft notification to the ACCC, we made no claim that these price increases are necessary to cover an increase in costs which can be attributed to an increase in the amount of compensation payments. As such we believe the existing compensation limit of \$50 is not a relevant component of the current price notification. Furthermore, given that Section 34 of our Act provides statutory protection in the event of loss or damage to items sent via the letter service, should Australia Post attempt to increase the compensation limits the ACCC may question whether the proposed prices are recovering the efficient costs of providing the reserved service (given the statutory immunity) and whether such a change would have a negative impact upon other competitive offers (eg. would it result in customers moving towards the reserved services).

You have suggested that Australia Post should consider adopting the Royal Mail model whereby the compensation amount is based on a multiple of the basic postage rate. Under our current compensation framework, compensation of up to \$50 in addition to a refund for any postage paid is available to customers sending ordinary items. Australia Post also has the discretion to pay compensation in excess of this amount where this is warranted by the circumstances of the particular claim. Given that the compensation provided by Royal Mail is in the form of 6 first class letter stamps for eligible letters, which equates to a much lower value than the amount offered by Australia Post, we see no merit in adopting this alternative compensation scheme.

In addition to our comments on your draft report I would also take this opportunity to provide some feedback on Mr Brent's letter of 26 October 2009 (ref: 2009-300007).

In this letter it is stated that "...compensation is a cost of providing the reserved services". As advised in our previous correspondence regarding this issue, there is no provision in our Act which stipulates that the Corporation is obliged to offer compensation for ordinary mail items. Australia Post offers a

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basic level of compensation for ordinary letters and parcels for the benefit of our customers and to differentiate our services from those of our competitors. The setting of these compensation limits is entirely at Australia Post's discretion.

Like many commercial organisations we offer a variety of products/services designed to meet a range of market needs, including the ability for our customers to purchase a level of cover that aligns with the value of the items being sent. In this way the cost is met by those who wish to purchase the service and therefore not subsidised by postal users in general.

In summary it is important to note that the bulk of compensation claims for mail items relate to parcels which are provided by Australia Post in a fully competitive environment. This would support our view that the value of items sent via the letter service is generally much less than those being sent as parcels. Nevertheless Australia Post offers the same amount of compensation for both letters (which includes reserved letters) and parcels.

In addition, given that the average compensation payout in the 2008/09 period was considerably less than \$50 we believe that there is no justification for changing the current limit at this time.

In regard to your specific recommendations, we have provided our responses in the attached. I trust that the information provided will be of assistance in this investigation. Should you wish to discuss further please contact me on (03) 9106 7115.

Yours sincerely



Paul Burke
Acting Corporate Secretary

Attachment

Recommendation 1

Australia Post should conduct a formal review of the amount of compensation it pays for loss and damage in the post to ordinary items as soon as practicable. The review should at least address the following:

- Identify the rationale for the figure being set at \$50 in 1987
- Review whether that rationale still holds good independently of the compensation levels payable for other services, and if not why not
- If that rationale still holds good, identify the compensation level that would be required to fulfil the same purpose at 2009 values

Response

It would not be appropriate for any review of Australia Post's compensation framework to take 1987 as a reference point.

Australia Post's structure and obligations were fundamentally changed in 1989 when the organisation became incorporated with a commercial charter. Prior to that Australia Post was a break-even Commission. To review from 1987 would suggest an analysis /critique of change that was driven by government policy which would be inappropriate for Australia Post.

Notwithstanding this and based on the information provided above we do not currently believe that a formal review of our compensation framework is justified.

Recommendation 2

Australia Post should, as part of its current notification to the ACCC of a proposed increase in the basic postage rate, draw this report to the ACCC's attention and should provide the ACCC with sufficient information to enable the ACCC to consider the implications of the existing or any proposed compensation arrangements for the proposed increase.

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Response

The level of compensation offered is not a relevant component of the Australia Post's letter price notification. The amount of compensation payments for domestic reserved letters is immaterial in the context of the total cost base for domestic reserved letters (the assessment of which the ACCC uses to determine the merits of a price notification).

Recommendation 3

Australia Post should incorporate information about its compensation arrangements and how they have changed over the relevant period in any future price notification to the ACCC.

Response

Similar to Recommendation 2 above the level of compensation offered by Australia Post is not a relevant component of any current or future price notification. Put simply, the amount of compensation payable for domestic reserved letters is immaterial in the context of the total cost base for domestic reserved letters.

Such action would only be applicable if one of the justifications for the increase in price was to offset an increase in the level of compensation payments and that such compensation payments were part of an efficient cost base. i.e. Australia Post was not passing on higher compensation payments as price increases to other postal users. This is not the case.

ABBREVIATIONS AND ACRONYMS

ACCC	Australian Competition and Consumer Commission
APC Act	<i>Australian Postal Corporation Act 1989</i>
Basic letter service	Collection and delivery of letters that conform to the following criteria: <ul style="list-style-type: none">(a) does not weigh more than 250 grams(b) not more than 5mm thick(c) other 2 dimensions form a rectangle:<ul style="list-style-type: none">(i) 2 of whose sides are shorter than the other sides; and(ii) the shorter sides of which are not more than 122 mm long; and(iii) the longer sides of which are not more than 237 mm long; and(iv) the adjacent sides of which are in the ratio of 1 to at least 1.414.
COD	Cash on delivery
CPI	Consumer price index, which measures the changing value of money over time by comparing how the dollar cost of a fixed selection of goods changes over the years
Extra Cover	Formerly known as insurance, a service by which customers can, for a fee, increase the maximum level of compensation payable for COD or registered post items
mm	Millimetre
Ordinary articles	Postal articles that have not been sent by the registered or COD services
Reserved services	Postal services that, under the provisions of the APC Act, only Australia Post may provide—broadly speaking, the basic letter service within Australia, except where a charge of at least four times the charge for Australia Post’s basic letter service is levied.