

UNITED STATES OF AMERICA  
POSTAL REGULATORY COMMISSION  
WASHINGTON, DC 20268-0001

Before Commissioners:

Ruth Y. Goldway, Chairman;  
Mark Acton, Vice Chairman; and  
Robert G. Taub

Market Test of Experimental Product-  
Customized Delivery

Docket No. MT2014-1

ORDER AUTHORIZING CUSTOMIZED DELIVERY MARKET TEST

(Issued October 23, 2014)

I. INTRODUCTION

On September 23, 2014, the Postal Service filed a notice, pursuant to 39 U.S.C. § 3641, announcing its intent to conduct a market test of an experimental product called Customized Delivery.<sup>1</sup> Customized Delivery is a package delivery service offering that will provide customers with delivery of groceries and other prepackaged goods, primarily during a 3 a.m. to 7 a.m. delivery window. *Id.* at 1. The Postal Service also requested an exemption from the \$10 Million Adjusted Limitation.<sup>2</sup>

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<sup>1</sup> Notice of the United States Postal Service of Market Test of Experimental Product – Customized Delivery, September 23, 2014 (Notice).

<sup>2</sup> *Id.* at 7; see 39 U.S.C. § 3641(e)(2) and 39 C.F.R. § 3035.16. “\$10 Million Adjusted Limitation” means \$10 million of total revenue as adjusted for inflation under 39 U.S.C. § 3641(g) and 39 C.F.R. § 3035.15. Total revenues anticipated or received by the Postal Service from a market test may not exceed the \$10 Million Adjusted Limitation unless the Commission grants an exemption under 39 U.S.C. § 3641(e)(2) and 39 C.F.R. § 3035.16.

The Commission finds that the Customized Delivery market test meets the requirements of 39 U.S.C. § 3641(b) and therefore authorizes the market test to proceed. However, the Commission denies the request for an exemption from the \$10 Million Adjusted Limitation as premature due to the lack of financial data to estimate revenues for Customized Delivery. The Postal Service may resubmit its request for an exemption from the \$10 Million Adjusted Limitation once it collects and reports to the Commission sufficient data to calculate the total revenue received and estimate the additional revenue anticipated for each fiscal year of the market test.

## II. BACKGROUND

On August 18, 2014, the Postal Service began conducting operational testing for early morning grocery delivery in 38 ZIP Codes.<sup>3</sup> The operational test involves the retailer dropping groceries packed into branded totes, some of which are chilled or include freezer packs, between 1:30 a.m. and 2:30 a.m. directly into Postal Service destination delivery units (DDU). Notice at 2. The totes, which have a Quick Response (QR) code on the outside, are all the same size and color. *Id.* The retailer provides a manifest file to the Postal Service, which contains the address and QR code for each tote. *Id.* The Postal Service uses this file to dynamically route totes and create a line of travel for each route. *Id.*

City Carrier Assistants (CCAs) use smart phones to scan the totes, which are sorted by route and delivery order and back-loaded onto a truck for delivery. *Id.* at 3. Deliveries occur from 3 a.m. to 7 a.m. and are left in a customer-designated location for delivery. *Id.* Totes are scanned to provide tracking and visibility from drop-off through delivery. *Id.* The public can easily recognize CCAs, who wear postal uniforms and lighted caps as safety measures. *Id.*

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<sup>3</sup> Notice at 2; Responses of the United States Postal Service to Chairman's Information Request No. 1, Questions 3 and 5, with Portions Under Seal, October 9, 2014, at question 5 (Responses to CHIR No. 1, questions 3 and 5).

During the operational test, the Postal Service delivered an average of 160 totes per day (1 to 4 per applicable address) for the 38 ZIP Codes included in the testing. *Id.* Through the market test, the Postal Service seeks to test and develop a long-term scalable solution to expand the operational test of Customized Delivery to additional major metropolitan markets nationwide and test other possible delivery windows throughout the day. *Id.* The market test is scheduled to begin on or shortly after October 24, 2014 and last for two years. *Id.* at 6.

### III. PROCEDURAL HISTORY AND COMMENTS

The Postal Service filed the Notice, with some portions of the supporting information and data filed under seal, on September 23, 2014. The Commission noticed the filing and gave interested persons the opportunity to submit comments on whether the Postal Service's filing is consistent with the policies of 39 U.S.C. § 3641.<sup>4</sup> On September 30, 2014, Chairman's Information Request No. 1 was issued to seek clarification on the proposed market test.<sup>5</sup> That same day, the Public Representative submitted a Motion for Issuance of Information Request.<sup>6</sup>

Chairman's Information Request No. 2 was issued on October 2, 2014.<sup>7</sup> On October 8, 2014, the Postal Service submitted partial responses to CHIR No. 1.<sup>8</sup> On October 9, 2014, the Public Representative and the Taxpayers Protection Alliance

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<sup>4</sup> Notice and Order Concerning Market Test of Experimental Product—Customized Delivery, September 25, 2014 (Order No. 2197).

<sup>5</sup> Chairman's Information Request No. 1, September 30, 2014 (CHIR No. 1).

<sup>6</sup> Public Representative Motion for Issuance of Information Request, September 30, 2014.

<sup>7</sup> Chairman's Information Request No. 2, October 2, 2014 (CHIR No. 2).

<sup>8</sup> Responses of the United States Postal Service to Chairman's Information Request No. 1, October 8, 2014 (Responses to CHIR No. 1, questions 1-2 and 4). The Postal Service filed an accompanying motion for late acceptance. Motion of the United States Postal Service for Late Acceptance of Responses to Chairman's Information Request No. 1, October 8, 2014. The Motion is granted.

(TPA) submitted comments on the proposed market test.<sup>9</sup> No other persons filed comments. That same day, the Postal Service submitted responses to the remaining questions in CHIR No. 1.<sup>10</sup>

On October 10, 2014, Chairman's Information Request No. 3 was issued to facilitate the Commission's evaluation of "market disruption" of the proposed market test under 39 U.S.C. § 3641(b)(2).<sup>11</sup> That same day, the Postal Service submitted responses to CHIR No. 2.<sup>12</sup> On October 14, 2014, the Commission's rules governing market tests of experimental products became effective.<sup>13</sup> On October 17, 2014, the Postal Service submitted responses to CHIR No. 3.<sup>14</sup>

The Public Representative supports the market test and believes that the market test is in the public interest. PR Comments at 1. However, she contends that the current record is inadequate for the Commission to evaluate market disruption under 39 U.S.C. § 3641(b)(2). *Id.* at 1-6. She proposes a framework for evaluating market

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<sup>9</sup> Public Representative's Comments, October 9, 2014 (PR Comments); Comments of Taxpayers Protection Alliance, October 9, 2014 (TPA Comments).

<sup>10</sup> Responses to CHIR No. 1, questions 3 and 5. The Postal Service filed an accompanying motion for late acceptance. Motion of the United States Postal Service for Late Acceptance of Responses to Chairman's Information Request No. 1, Questions 3 and 5, October 9, 2014. The Motion is granted.

<sup>11</sup> Chairman's Information Request No. 3, October 10, 2014 (CHIR No. 3).

<sup>12</sup> Responses of the United States Postal Service to Chairman's Information Request No. 2, October 10, 2014 (Responses to CHIR No. 2). The Postal Service filed an accompanying motion for late acceptance. Motion of the United States Postal Service for Late Acceptance of Responses to Chairman's Information Request No. 2, October 10, 2014. The Motion is granted.

<sup>13</sup> See 79 FR 54552 (September 11, 2014). The market test rules became effective after the Notice was filed. The D.C. Circuit has held that rules do not operate retroactively, even when applied to transactions predating their institution, if they are procedural rules that regulate only "secondary rather than primary conduct." 292 F.3d 849, 859 (D.C. Cir. 2002). Applying new rules to pending cases has no retroactive effect if the new rules are "substantively consistent with prior regulations or prior agency practices...." *Id.* at 860. Thus, the market test rules do not operate retroactively because they are mostly procedural in nature and are substantively consistent with prior Commission practice regarding market tests. Nonetheless, the Commission reviews and approves the Customized Delivery market test based on 39 U.S.C. § 3641 and Commission precedent in past orders. Going forward, however, the Commission will apply the market test rules to future filings concerning the Customized Delivery market test, including notices expanding the market test to other geographic areas.

<sup>14</sup> Responses of the United States Postal Service to Chairman's Information Request No. 3, October 17, 2014 (Responses to CHIR No. 3).

disruption based on Commission precedent and general principles of antitrust law. *Id.* at 2-4. Based on that framework, she concludes that insufficient information exists to assess whether the market test will cause market disruption. *Id.* 4-6. She suggests that the Commission may analyze market disruption by evaluating the operational test. *Id.* at 6-9. In addition, she argues that the Postal Service should provide advance notice of changes to the market test that may impact the market disruption analysis, including expanding the market test to other geographic areas. *Id.* at 9-10.

The Public Representative also recommends that the Commission deny the request for an exemption from the \$10 Million Adjusted Limitation, include the operations test period when calculating the market test's revenue and duration limitations, and expand the scope of data collection. *Id.* at 10-12.

TPA argues that the Customized Delivery market test should not move forward. It asserts that expanding grocery delivery services to additional markets will harm private providers. TPA Comments at 1. It argues that the Commission should not approve the market test until it obtains financial details of the expansion and determines the market test's effect on the Postal Service and American businesses. *Id.*

#### IV. COMMISSION ANALYSIS

Based on a review of the record, including the Postal Service's filing, the comments received, and responses to CHIRs, the Commission concludes that the Customized Delivery market test meets the requirements of 39 U.S.C. § 3641(b). Accordingly, the market test is authorized to proceed. However, the Commission denies the request for an exemption from the \$10 Million Adjusted Limitation without prejudice as premature due to the lack of financial data to estimate revenue for Customized Delivery. The Postal Service may resubmit its request for exemption once it collects and reports to the Commission sufficient data to calculate the total revenue received and estimate the additional revenue anticipated for each fiscal year of the market test.

Below the Commission analyzes applicable statutory and regulatory provisions to ensure that the Customized Delivery market test meets these requirements.

A. 39 U.S.C. § 3641(b) Conditions

The Postal Service may not test an experimental product under 39 U.S.C. § 3641 unless the experimental product satisfies three conditions: (1) the experimental product is, from the viewpoint of mail users, significantly different from all Postal Service products offered within the past two fiscal years; (2) the introduction or continued offering of the experimental product will not create an unfair or otherwise inappropriate competitive advantage for the Postal Service or any mailer, especially regarding small business concerns; and (3) the Postal Service correctly identifies the experimental product as either market dominant or competitive. 39 U.S.C. § 3641(b). As discussed below, the Commission finds that Customized Delivery meets these three conditions.

1. Significantly Different Product

The Commission finds that Customized Delivery is significantly different from all other Postal Service products offered within the past two fiscal years, and therefore satisfies section 3641(b)(1). Customized Delivery may be considered analogous to Metro Post, a same-day delivery service that is currently being tested under the Metro Post market test.<sup>15</sup> However, as illustrated in the table below, Customized Delivery materially differs from Metro Post based on key features of each experimental product.

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<sup>15</sup> See Docket No. MT2013-1, Order No. 1539, Order Approving Metro Post Market Test, November 14, 2012.

Feature	Customized Delivery	Metro Post
Delivery Window	Retailers can specify a unique timeframe for delivery	Retailers cannot specify a timeframe for delivery
Delivery Location and Customer Acceptance	Items are delivered directly to a customer's door without disturbing the customer	Items are delivered where mail and packages would normally be delivered to customer
Undeliverable Items	Returned to shipper	Rolled into next day delivery
Delivery Instructions	Customers may provide specific delivery instructions	Customers may not provide specific delivery instructions
Prices	Postal Service negotiates prices with each customer based on their pickup schedules	Prices are fixed
Groceries <sup>16</sup>	Perishables can be delivered	Perishables cannot be delivered

Notice at 4; Responses to CHIR No. 1, questions 1-2 and 4, question 4.

The Commission received no comments addressing whether Customized Delivery is significantly different from other Postal Service products. Given that Customized Delivery differs from all products offered by the Postal Service, including Metro Post, in terms of delivery features, prices charged, and items delivered, the Commission finds that Customized Delivery is, from the viewpoint of mail users, significantly different from other Postal Service products offered within the past two fiscal years.

## 2. Market Disruption

The Customized Delivery market test may not proceed unless the Commission finds that the "introduction or continued offering" of Customized Delivery will not create

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<sup>16</sup> In addition to perishable items, "groceries" include not only household items such as paper towels, bathroom tissue, diapers, and basic consumables, but also non-edible items typically found in retail grocery stores. Responses to CHIR No. 2, question 2.

market disruption, which is defined as “an unfair or otherwise inappropriate competitive advantage for the Postal Service or any mailer, particularly in regard to small business concerns....”<sup>17</sup> “Introduction or continued offering” requires the Commission to evaluate market disruption both at the beginning of the market test and throughout the duration of the market test to ensure continued compliance with 39 U.S.C. § 3641(b)(2). Based on the record before it, the Commission finds no indication that the introduction of Customized Delivery in the San Francisco metropolitan area will cause market disruption. To assess continued compliance with section 3641(b)(2), the Postal Service must notify the Commission, pursuant to 39 C.F.R. § 3035.6, if it expands the Customized Delivery market test to additional geographical areas.

a) Introduction of Customized Delivery

TPA argues the Postal Service’s expansion of grocery delivery to additional markets will hurt private businesses that cannot lower prices to compete with the Postal Service. TPA Comments at 1. The Public Representative proposes a framework for evaluating market disruption based on Commission precedent and principles of antitrust law. PR Comments at 2. She argues that the market disruption analysis begins by first identifying the relevant product and geographic market for Customized Delivery. The product market is determined by employing the hypothetical monopolist test, which “identifies reasonably substitutable products and competitors that if controlled by the monopolist would allow the monopolist to increase prices and profits.”<sup>18</sup> The geographic market is “the geographic area where the hypothetical monopolist can freely increase prices and profits without causing an influx of competition from outside sources.” PR Comments at 3 (citing Order No. 1448 at 25-26).

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<sup>17</sup> 39 U.S.C. § 3641(b)(2). “Small business concern” is defined in 39 C.F.R. § 3001.5(v).

<sup>18</sup> *Id.* at 2 (citing Docket Nos. MC2012-14 and R2012-8, Order No. 1448, Order Approving Addition of Valassis Direct Mail, Inc. Negotiated Service Agreement to the Market Dominant Product List, August 23, 2012, at 24-25).

The Public Representative explains that the next step in the market disruption analysis is to apply the rule of reason to evaluate whether Customized Delivery will create “an unfair or otherwise inappropriate competitive advantage for the Postal Service or any mailer, particularly in regard to small business concerns....” PR Comments at 3-4. The rule of reason analysis focuses on whether the behavior unreasonably restrains competition by reviewing the "anticompetitive effects" of the action.<sup>19</sup>

Based on this framework, the Public Representative concludes that insufficient information exists to assess whether Customized Delivery will cause market disruption because the relevant product and geographic markets have not been defined. PR Comments at 4. However, she asserts that the Commission may evaluate market disruption on a limited basis based on the operational test that began on August 18, 2014. *Id.* at 6. She defines the market as a set-window delivery of prepackaged groceries and other goods within the operational test area. *Id.* at 7. Applying the rule of reason analysis, she concludes that the market test is unlikely to cause competitive harm to the marketplace generally or to consumers specifically. *Id.* at 8. She argues that assuming prices for Customized Delivery are comparable to similar services and Customized Delivery does not provide enhancements or unique benefits, competitors, including small businesses, are unlikely to be harmed by the Postal Service entering the competitive market. *Id.* at 8-9.

In this case, the Commission will apply a similar framework for analyzing market disruption. That framework begins by first identifying the relevant market for the Customized Delivery market test. For market tests, the relevant market is identified by examining the description of the experimental product and the geographic area(s) where the Postal Service intends to offer the experimental product during the market test duration. In this case, Customized Delivery can be described as a set-window delivery of groceries and other prepackaged goods. Notice at 1. At the Commission’s

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<sup>19</sup> Docket No. RM2013-4, Order No. 1739, Notice of Proposed Rulemaking Establishing Rules Pursuant to 39 U.S.C. § 404a, June 5, 2013, at 7.

request, the Postal Service identified the geographic area(s) where it intends to offer Customized Delivery during the market test. It states that the market test will begin in the San Francisco metropolitan area.<sup>20</sup> Thus, the relevant market for the Customized Delivery market test is the set-window delivery of groceries and other prepackaged goods in the San Francisco metropolitan area.

The second step of the market disruption analysis is to identify businesses that offer similar products or services in the relevant market. In this case, these businesses are grocery delivery service providers operating in the San Francisco metropolitan area. At the Commission's request, the Postal Service identified several grocery delivery service providers, such as Safeway, Vons, Instacart (Whole Foods), Giant (Peapod), Fresh Direct, and Urban Grocery. *Id.*, question 4.

The third step of the market disruption analysis is to evaluate whether the introduction or continued offering of the experimental product will create "an unfair or otherwise inappropriate competitive advantage for the Postal Service or any mailer...." with regard to the service providers identified in step 2. See 39 U.S.C. § 3641(b)(2). In this case, the Commission must determine whether Customized Delivery will provide an unfair or otherwise inappropriate competitive advantage with regard to other grocery delivery service providers operating in San Francisco. For example, if prices for Customized Delivery were set significantly below prices offered by existing grocery delivery service providers operating in San Francisco, the Postal Service and the retail partner might have "an unfair or otherwise inappropriate competitive advantage" over other grocery delivery service providers who are unable to lower the prices for their services.

The Postal Service asserts that Customized Delivery will not cause market disruption because "[t]he prices offered by competitors for grocery delivery typically fall

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<sup>20</sup> Responses to CHIR No. 3, questions 1 and 2. The Postal Service further states that it may extend the market test to other geographic areas, such as Phoenix, Arizona; Las Vegas, Nevada; and Portland, Oregon. As discussed in Section IV.A.2.b. below, the Postal Service must provide advance notice to the Commission, pursuant to 39 C.F.R. § 3035.6, if it expands the market test to additional geographic areas.

within the price range that the Postal Service intends to test.” Notice at 5. It explains that delivery fees for similar grocery delivery service providers can range from as low as \$3.99 to \$15.99. Responses to CHIR No. 3, question 4. It states that the lowest end of the price range for the Customized Delivery market test would not provide the Postal Service overwhelming market power in the grocery delivery market. *Id.*

The Commission has evaluated the Postal Service’s pricing plans filed under seal as well as a sampling of similar grocery delivery service providers. The Commission finds that the prices offered by grocery delivery service providers operating in San Francisco are comparable to the price range the Postal Service intends to test. Therefore, Customized Delivery is unlikely to provide the Postal Service or the retail partner an unfair or inappropriate competitive advantage. Moreover, the prices charged by the Postal Service for Customized Delivery will have limited impact since they will only be effective for the duration of the market test. Concerns about the pricing of Customized Delivery will also be addressed if and when the Postal Service requests that Customized Delivery become a permanent product. In that case, the Postal Service’s prices will be further constrained by the statutory requirement that Customized Delivery must cover its costs. See 39 U.S.C. § 3633(a)(2).

The fourth step of the market disruption analysis involves examining the impact of the market test on “small business concerns,” as defined in 39 C.F.R. § 3001.5(v), in the relevant market. In this case, “small business concerns” mean Courier and Express Delivery Services companies with 1,500 or fewer employees and Local Messengers and Local Delivery companies with annual receipts of \$27.5 million or less. See 39 C.F.R. § 121.201, Section 48-49, Subsector 492 (applicable Small Business Administrative size standards).

The Postal Service argues that Courier and Express Delivery Service companies will continue to operate within the emerging market for grocery delivery. Responses to CHIR No. 2, question 1. It asserts that retail grocery stores and other companies have and will continue to use couriers or smaller delivery companies for delivery. *Id.* It contends that couriers and smaller delivery companies specialize in delivering

time-sensitive medical items as well as business, legal, and financial documents, which fall outside the intended scope of Customized Delivery. *Id.* The Commission finds these Postal Service assertions reasonable.

While not dispositive, no small business concern opposes the market test. Furthermore, 39 U.S.C. § 3641 contains additional safeguards to ensure that market disruption will not occur. The Commission is authorized to limit the amount of revenues the Postal Service may obtain from any particular geographic market as necessary to prevent market disruption. 39 U.S.C. § 3641(e)(1); 39 C.F.R. § 3035.17. If necessary, the Commission may also cancel the market test or take other action that it deems appropriate. 39 U.S.C. § 3641(f); 39 C.F.R. § 3035.12.

Applying the framework discussed above, the Commission finds that the record contains no indication that the introduction of Customized Delivery will “create an unfair or otherwise inappropriate competitive advantage for the Postal Service or any mailer, particularly in regard to small business concerns....” 39 U.S.C. § 3641(b)(2). Customized Delivery therefore satisfies the “market disruption” condition in 39 U.S.C. § 3641(b)(2).

b) Continued Compliance with Section 3641(b)(2)

The Public Representative contends that the relevant market must be redefined if the Postal Service expands the market test to geographic areas beyond San Francisco because the expansion may affect the market disruption analysis under 39 U.S.C. § 3641(b)(2). PR Comments at 10. She recommends that the Postal Service provide advance notice of an expansion, as well as changes to the Customized Delivery product, pursuant to 39 C.F.R. § 3035.6, so that the Commission may consider whether these changes affect compliance with 39 U.S.C. § 3641(b)(2). *Id.* at 9-10.

The Commission cannot assess continued compliance of the Customized Delivery market test with section 3641(b)(2) without knowing the additional geographic area(s) in which the Postal Service will offer Customized Delivery during the market test’s duration. Thus, the Postal Service must provide advance notice to the

Commission, pursuant to 39 C.F.R. § 3035.6, if it intends to expand the Customized Delivery market test to additional geographical areas.<sup>21</sup> This requirement is consistent with the Commission's directive for the Metro Post market test. Order No. 1539 at 8. The Commission will then evaluate whether the proposed expansion impacts Customized Delivery's compliance with section 3641(b)(2).

c) Future Filings

The Commission agrees with the Public Representative that the Notice, as filed, does not provide sufficient information for the Commission to evaluate market disruption under 39 U.S.C. § 3641(b)(2). However, the Postal Service offered additional information at the Commission's request in its responses to CHIR Nos. 1, 2, and 3. To facilitate the Commission's evaluation of market disruption in future market tests or expansions of the Customized Delivery market test, future notices of market tests should provide, at a minimum:

- The geographic area(s) where the Postal Service intends to offer the experimental product during the market test duration;
- Examples of businesses that offer similar products or services in these geographic areas;
- The range of prices these businesses charge for similar products and services; and
- A description of the impact of the market test on small business concerns.

An example of the level of detail requested for this information can be found in the Responses to CHIR No. 2, question 1 and Responses to CHIR No. 3.

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<sup>21</sup> 39 C.F.R. § 3035.6 also requires the Postal Service to provide advance notice of other material changes made to the market test or experimental product that may affect compliance with 39 U.S.C. § 3641.

### 3. Correct Categorization

The Postal Service categorizes Customized Delivery as a competitive product. Notice at 6. It asserts that Customized Delivery is designed for packages that do not fall under the Private Express statutes. *Id.* It submits that Customized Delivery is another component of the highly-competitive package services market. *Id.*

Under 39 U.S.C. § 3641(b)(3), a market test must be characterized as market dominant or competitive consistent with 39 U.S.C. § 3642(b)(1). Section 3642(b)(1) states that market dominant products are products that “the Postal Service exercises sufficient market power that it can effectively set the price of such product substantially above costs, raise prices significantly, decrease quality, or decrease output, without risk of losing a significant level of business to other firms offering similar products. The competitive category of products shall consist of all other products.” Neither commenter opposes categorizing Customized Delivery as a competitive product. The Commission finds that the Postal Service has properly identified Customized Delivery as a competitive product because the presence of other grocery delivery service providers described in Section IV.A.2, above, minimizes the likelihood that the Postal Service will be able to set prices for Customized Delivery substantially above costs, raise prices significantly, or decrease quality and output without risking loss of significant business to other grocery delivery service providers. See 39 U.S.C. § 3642(b)(1). Customized Delivery therefore satisfies the “correct categorization” condition in 39 U.S.C. § 3641(b)(3).

#### B. Other Statutory and Regulatory Requirements

##### 1. Duration

A market test may not exceed 24 months in duration unless the Commission authorizes an extension for up to an additional 12 months. 39 U.S.C. § 3641(d); 39 C.F.R. § 3035.10. The Postal Service states that the Customized Delivery market test will begin on or shortly after October 24, 2014 and will run for two years unless the

Postal Service requests an extension, establishes Customized Delivery as a permanent product, or terminates the market test early. *Id.* at 6. As discussed above, a related operational test began on August 18, 2014.

The Public Representative argues that the Postal Service operated without proper authority when it conducted the operational testing. PR Comments at 11. She notes that the Postal Service is required to provide 30 days advance written notice to the Commission and in the *Federal Register* before initiating a market test. *Id.* at 11 (citing 39 U.S.C. § 3641(c)(1)). She contends that a market test is the only vehicle for the Postal Service to test an experimental product and that the operational test violated section 3641(c)(1). *Id.* She asserts that renaming an unapproved market test as an “operations test” creates an end-run around several key requirements in 39 U.S.C. § 3641, including duration and revenue limitations. *Id.* at 11-12. She recommends that the duration of and revenues from the operational test should be included when determining the market test’s duration and revenue limitations. *Id.*

The Postal Service distinguishes “operational tests” from “market tests” by noting that operational tests do not yield new revenues and are limited in geographic scope and duration. Responses to CHIR No. 1, question 3 and 5, question 5. It asserts that operational tests are designed for the Postal Service to evaluate whether it has the operational capabilities to potentially introduce a new service or product offering as an experimental or permanent product. *Id.*

Whether the testing of a particular potential product should be classified as a market test or an operational test is not inherently clear. On the one hand, the Postal Service needs to be able to evaluate whether it is operationally viable for it to offer a new product prior to determining whether it makes sense, from an operations perspective, to consider offering such a new product for potential customer demand testing. If such a test is deemed a market test for purposes of 39 U.S.C. § 3641, the Postal Service would be required to file a notice proposing a market test with the Commission virtually every time it seeks to test its operational limitations. On the other hand, if the Postal Service were permitted to offer new products under the guise of

expansive, wide ranging operational tests without following the requirements of section 3641, the purposes of section 3641 would be frustrated.

The appropriate balance between the Postal Service's flexibility to test its operational capabilities and the Commission's responsibility to enforce the statutory limitations on market tests lies in the middle of these two extremes. Consequently, the Commission finds that the testing of a potential new product does not rise to the level of a market test under 39 U.S.C. § 3641 when all of the following conditions are met: (1) the Postal Service does not collect any new revenue in connection with the test, (2) the test is short enough in duration such that it will not cause market disruption, (3) the test is limited in geographic scope, and (4) the test is designed to assess the Postal Service's operational capabilities – as opposed to evaluating potential customer interest or marketing efforts. Such testing is more operational in nature than a market test under section 3641(b) which is designed to gauge customer demand or interest.<sup>22</sup>

In this case, the Commission finds that the Customized Delivery operational test does not rise to the level of a market test because the Postal Service is not collecting any revenues in connection with the test, the duration of the operational test is short enough such that it will not cause market disruption,<sup>23</sup> the operational test is limited in scope to 38 ZIP Codes, and the Postal Service represents that the operational test is designed to test operational capabilities rather than potential customer interest or marketing efforts.

As a result, the operational test that began on August 18, 2014 does not rise to the level of a market test under 39 U.S.C. § 3641. Consequently, the Customized Delivery market test's duration will begin on the date that the Postal Service notifies the

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<sup>22</sup> The Postal Service previously filed notice of its intent to conduct the Samples Co-Op Box market test. Notice of the United States Postal Service of Market Test of Experimental Product--Samples Co-Op Box, March 29, 2010. The market test was completed in a single week, and the Postal Service did not receive any revenue from the market test. *Id.* at 8. The Postal Service noted that the status of Samples Co-Op Box as a market test was unclear, but indicated it was filing the notice in the interest of transparency. *Id.* at 2-3.

<sup>23</sup> See also *supra* Section IV.A.2. for the Commission's market disruption analysis.

Commission that the Customized Delivery market test started and will end two years later unless the market test is extended or cancelled.<sup>24</sup>

## 2. Exemption from Revenue Limitation

Total revenues anticipated or received by the Postal Service from a market test in any fiscal year may not exceed the \$10 Million Adjusted Limitation unless the Commission grants an exemption. 39 U.S.C. § 3641(e); 39 C.F.R. § 3035.15(b). The Commission shall approve a request for an exemption from the \$10 Million Adjusted Limitation if it determines that the experimental product: (1) is likely to benefit the public and meet an expected demand; (2) is likely to contribute to the financial stability of the Postal Service; and (3) is unlikely to result in unfair or otherwise inappropriate competition. 39 U.S.C. § 3641(e)(2); 39 C.F.R. § 3035.16. If the Commission grants an exemption, total revenues anticipated or received by the Postal Service from a market test may not exceed the \$50 Million Adjusted Limitation in any fiscal year.<sup>25</sup>

The Postal Service requests an exemption from the \$10 Million Adjusted Limitation, noting that revenues may exceed the limitation if adoption of Customized Delivery proves to be particularly strong. Notice at 7. However, it states that “[t]he exact revenue and volume is difficult to predict, as the success of the market test depends on the number of participating retailers, the scope of their businesses, and ultimately, the demand for grocery delivery among consumers in the marketplace.” *Id.* It asserts that the Customized Delivery market test is likely to benefit the public, meet an expected demand, and contribute to the Postal Service’s financial stability by generating package deliveries that do not currently move within the postal system. *Id.*

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<sup>24</sup> See 39 U.S.C. § 3641(d)(2) and 39 C.F.R. § 3035.11; 39 U.S.C. § 3641(f) and 39 C.F.R. § 3035.12.

<sup>25</sup> *Id.* “\$50 Million Adjusted Limitation” means \$50 million total revenue as adjusted for inflation under 39 U.S.C. § 3641(g) and 39 C.F.R. § 3035.16. If the Commission grants a request for an exemption from the \$10 Million Adjusted Limitation, total revenues anticipated or received by the Postal Service from a market test may not exceed the \$50 Million Adjusted Limitation in any fiscal year. 39 U.S.C. § 3641(e)(2); 39 C.F.R. § 3035.16.

The Public Representative recommends that the Commission deny the request for an exemption from the \$10 Million Adjusted Limitation without prejudice because the record lacks sufficient information to support the findings the Commission must make under 39 U.S.C. § 3641(e)(2). PR Comments at 10. She argues that the Postal Service failed to explain how Customized Delivery is unlikely to result in unfair or otherwise inappropriate competition. *Id.* at 10-11. She also contends that the request is premature and that denying the request will enable the Postal Service to gather sufficient data to assess whether an exemption is necessary. *Id.* at 11 n.23.

The Commission denies the request for an exemption from the \$10 Million Adjusted Limitation without prejudice as premature. The Postal Service concedes that total projected revenues for the market test are difficult to calculate because prices may be determined based on markets, delivery density, number of shippers, and the ability of shippers to deliver goods to Postal Service facilities. Responses to CHIR No. 1, questions 1-2 and 4, question 2. While the demand for grocery delivery services may increase, neither the Postal Service nor the Commission can accurately project at this time whether the demand will necessitate an exemption from the \$10 Million Adjusted Limitation. The Commission is prepared to review an exemption request for this market test if the Postal Service can demonstrate that revenues are likely to exceed the \$10 Million Adjusted Limitation.

The Postal Service may resubmit its request for an exemption from the \$10 Million Adjusted Limitation once it collects sufficient data to calculate the total revenue received and estimate the additional revenue anticipated for each fiscal year of the market test.<sup>26</sup>

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<sup>26</sup> See 39 C.F.R. § 3035.16(f)(2) and (3). A request for an exemption from the \$10 Million Adjusted Limitation must also quantify the product specific costs associated with the development of the market test, which are costs incurred before the market test is implemented. *Id.* § 3035.16(f)(4).

### 3. Data Collection Plan

The Notice includes a proposed data collection plan for the Customized Delivery market test as required by 39 C.F.R. § 3035.3(a)(2)(vi). Notice at 8. The Postal Service proposes to collect data on the volume of packages delivered via Customized Delivery; total revenue generated; work hours, travel times, and cost data; and administrative and start-up cost data. *Id.* It is prepared to report on the results of the data collection to the Commission. *Id.*

The Public Representative argues that the Commission should expand the scope of the data collection plan by directing the Postal Service to collect and report data as envisioned in 39 C.F.R. § 3035.20. PR Comments at 12. She recommends that the Commission clarify that consistent with 39 C.F.R. § 3035.20, both volume and revenue data must be reported for each fiscal quarter, and revenue data must be disaggregated by geographic area. *Id.* She suggests that the Postal Service collect additional data on the number of totes, to be provided in an electronic file. *Id.* at 13. She asserts that the Postal Service should advise the Commission if it is unable to collect the required data and propose an alternative for the data in data collection reports. *Id.*

The Commission agrees that consistent with 39 C.F.R. § 3035.20, volumes and revenues must be reported by fiscal quarter, and total revenues must be disaggregated by geographic area. In addition, the Postal Service must report attributable costs incurred in conducting the Customized Delivery market test as well as the number of deliveries and any additional fees charged per delivery. *See id.* §§ 3035.20(a)(2), (b). The other data collection items suggested by the Public Representative could be useful in the Postal Service's efforts to determine if it should make Customized Delivery a permanent product. However, these items are not necessary for the Commission to monitor compliance with 39 U.S.C. § 3641.

In summary, the data collection plan for the Customized Delivery market test consists of the following:

- Total revenues generated from the market test by fiscal quarter, disaggregated by geographic area;

- Attributable costs incurred in conducting the market test, including product specific costs related to the administration of the market test and costs of dedicated delivery routes;
- Volumes of packages delivered via Customized Delivery by fiscal quarter;
- The number of deliveries made via Customized Delivery, along with any additional fees charged per delivery;
- Work hours, travel times, and other cost data; and
- Administrative and start-up cost data.

The Postal Service shall file the information required by the data collection plan in data collection reports. 39 C.F.R. § 3035.20(d). The Postal Service must file data collection reports within 40 days after the close of each fiscal quarter during which the market test is conducted. Data or information may be filed under protective conditions to prevent disclosure of commercially sensitive material.

## V. CONCLUSION

For the reasons discussed above, the Commission finds that the Customized Delivery market test meets the requirements of 39 U.S.C. § 3641(b) and therefore authorizes the market test to proceed. The Commission denies the request for an exemption from the \$10 Million Adjusted Limitation without prejudice as premature due to the lack of financial data to estimate revenue for Customized Delivery. The Postal Service may resubmit its request for exemption once it collects and reports to the Commission sufficient data to calculate the total revenue received and estimate the additional revenue anticipated for each fiscal year of the market test.

## VI. ORDERING PARAGRAPHS

*It is ordered:*

1. Based on the record before it, the Commission finds that the proposed Customized Delivery market test is consistent with 39 U.S.C. § 3641(b) and authorizes the market test to proceed in the San Francisco metropolitan area.
2. The Postal Service shall promptly notify the Commission of the effective date of the Customized Delivery market test. It will expire two years from that date unless the market test is extended or cancelled as described in the body of this Order.
3. The Postal Service must provide advance notice to the Commission, pursuant to 39 C.F.R. § 3035.6, if it expands the Customized Delivery market test to additional geographic areas.
4. The Postal Service's request for an exemption from the \$10 Million Adjusted Limitation is denied without prejudice as premature.
5. The Postal Service shall file data collection reports, as described in the body of this Order, within 40 days after the close of each fiscal quarter during which the market test is offered.
6. Revisions to the competitive product list and the Mail Classification Schedule appear below the signature of this Order and are effective immediately.
7. The Secretary shall arrange for publication in the *Federal Register* of an updated product list reflecting the change made in this Order.

By the Commission.

Ruth Ann Abrams  
Acting Secretary

## CHANGE IN PRODUCT LIST

The following material represents changes to the product list codified in Appendix A to 39 C.F.R. part 3020, subpart A--Mail Classification Schedule. These changes reflect the Commission's order in Docket No. MT2014-1. The Commission used two main conventions when making changes to the product list. New text is underlined. Deleted text is struck through.

Part B—Competitive Products  
2000 Competitive Product List

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MARKET TESTS\*

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Customized Delivery

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## CHANGES TO THE MAIL CLASSIFICATION SCHEDULE

The following material represents a change to the Mail Classification Schedule. The Commission uses two main conventions when making changes to the Mail Classification Schedule. New text is underlined. Deleted text is struck through.

Part B—Competitive Products  
2000 Competitive Product List

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### MARKET TESTS\*

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#### Customized Delivery

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2800 Market Tests

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2803 Customized Delivery

#### Reference

Docket No. MT2014-1

PRC Order No. 2224, October 23, 2014

#### Expires

TBD

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