

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

COMPETITIVE PRODUCT PRICES
GLOBAL EXPEDITED PACKAGE SERVICES
NEGOTIATED SERVICES AGREEMENTS

Docket No.
CP2008-5

**UNITED STATES POSTAL SERVICE RESPONSE TO ORDER NO. 78 AND NOTICE
OF FILING INFORMATION RESPONSIVE TO PART 3020 OF THE COMMISSION'S
RULES OF PRACTICE AND PROCEDURE**

(June 10, 2008)

On June 3, 2008, the Commission issued Order No. 78, giving notice of the following actions by the Postal Service: (i) the filing under seal of a Governors' decision setting forth price ranges for Global Expedited Package Services (GEPS) contracts and modifying previously proposed descriptive language about such contracts in the Mail Classification Schedule (MCS), and (ii) the filing under seal of a GEPS negotiated service agreement (NSA) with a customer.¹ The Commission considered the Governors' decision as establishing, in essence, a "shell classification" for functionally equivalent GEPS agreements.² The Commission directed the Postal Service to (i)

¹ While the Postal Service notice of the Governors' GEPS decision cited 39 C.F.R. §§ 3015.5 (Regulation of Rates for Competitive Products, Rate or class not of general applicability) and 3020.90 (Requests Initiated by the Postal Service to Change the Mail Classification Schedule), its notice of a GEPS customer agreement cited only the former of these provisions. Order No. 78 concludes that the GEPS customer agreement will be classified as a new product and consolidates the consideration of both notices under Docket No. CP2008-5. Order No. 78 determines that the Commission will consider the GEPS contract as if it had been filed pursuant to 39 C.F.R. 3020, Subpart B (Requests Initiated by the Postal Service to Modify Product Lists Described within the Mail Classification Schedule), making the Commission's review of the consolidated dockets pursuant to Rule 3020.34 (Review). Having exercised its discretion to consolidate the two proceedings and construe them collectively as supporting a request to modify product lists, the Commission invited the Postal Service to supplement the materials previously filed.

² In Order No. 43, the Commission acknowledged that it might be appropriate to group functionally equivalent NSAs as a single product. PRC Order No. 43, at 57-58, 64, 75. In Order No. 78, the Commission repeated this acknowledgement insofar as functionally equivalent NSAs exhibit similar cost and market characteristics. PRC Order No. 78, at 2-3. With their "shell classification" decision, the

identify and list any contracts currently in existence that would no longer qualify as GEPS contracts under the changed classification language proposed by the Postal Service, along with those contracts' expiration dates; and (ii) provide a detailed explanation as to why GEPS contracts' expiration dates, without disclosing the identity of the customer, should not be made publicly available.

I. Filing under Part 3020, Subpart B of the Rules of Practice and Procedure

At the Commission's invitation, the Postal Service is providing additional supporting materials under Part 3020, subpart B of the Rules of Practice and Procedure. Attachment A is the supporting statement of Frank Cebello, Executive Director, Global Business Management, under Rule 3020.32. With this filing, the Postal Service provides information in support of a modification to the competitive products list for, as a product not of general applicability, the shell classification of GEPS Contracts described in language proposed by the Postal Service for inclusion in section 2610.2 of the MCS. The Cebello statement also articulates, alternatively, the impact of adding the GEPS contract filed in this docket to the competitive products list. If the GEPS shell classification is added to the competitive products list, then the GEPS contract filed in this docket would fit its criteria and would belong to the functionally equivalent grouping defined thereby.³

II. Identification of Existing GEPS Contracts

Governors have established a pricing formula that will reflect the costs of each contract meeting a common description. All GEPS contracts meeting the Governors' criteria will necessarily exhibit similar cost and market characteristics; therefore, all GEPS contracts will be functionally equivalent and may be classified according to the general product description. In this case, as is anticipated in future cases, the certification that accompanies the filing of the GEPS contract effectively fits that GEPS contract within the shell classification.

³ In conformance with Rule 3020.31(b) and (f) of the Commission's Rules of Practice and Procedure, the Postal Service has provided copies of the relevant Governors' decision, under seal, and applicable MCS section, with proposed changes, in previous filings on this docket. Mr. Cebello's statement, appended hereto as Attachment A, serves as the supporting justification required by Rule 3020.31(e).

In Order No. 78, the Commission directed the Postal Service to identify and list any contracts currently in existence that would no longer qualify as GEPS contracts under the classification changes supplied by the Postal Service, along with those contracts' expiration dates. The Postal Service recently published price incentives for Express Mail International and Priority Mail International customers that effectively supersede those previously established by customer-specific agreements.⁴ These published incentives became effective in May 2008. As previous GEPS contracts have expired, customers unable to meet the new capability criteria for GEPS contracts have availed themselves of the new published incentives. The Postal Service has identified one remaining GEPS contract in effect that would not meet the new eligibility criteria; this contract expires on July 31, 2008.⁵

III. Confidentiality

In Order No. 78, the Commission directed the Postal Service to provide a detailed justification for why it believes that GEPS contracts' expiration dates, without disclosing the customers' identities, should not be made publicly available. The Postal Service has no objection to the listing of expiration dates for GEPS contracts, because it does not regard this information, considered in isolation, to be commercially sensitive. The Postal Service notes, however, that new GEPS contracts do not contain specific expiration dates; rather, their dates of effectiveness and expiration depend upon favorable conclusion of proceedings before the Commission. For example, the GEPS contract before the Commission here will become effective upon the Postal Service's

⁴ See PRC Order No. 70, at 18-20.

⁵ This contract was executed before the effective date of Order No. 43, which established the Commission's ratemaking regulations for market dominant and competitive products. Because this contract is scheduled to expire in July and the customer needed additional time to implement changes to its mail preparation processes, the Postal Service chose not to terminate the contract prematurely.

notification to the customer that the Commission and any other relevant oversight bodies have approved the contract, and the contract will expire twelve months thereafter. Therefore, the Postal Service recommends use of docket numbers or some other unique identifier to distinguish GEPS contracts, should the shell classification not take effect.

The Postal Service nevertheless maintains that the names of GEPS customers should remain confidential, due to the substantial likelihood that the Postal Service's private competitors would use such information to target their efforts and undercut the Postal Service's prices. Because of this risk, the Postal Service regards GEPS customer identities as commercially sensitive information that should remain in the non-public annex for this consolidated docket.

IV. Classification Criteria

In the Governors' decision filed in Docket No. CP2008-4, the Governors made certain changes to the classification criteria for GEPS contracts, including higher capacity thresholds. In Order No. 78, the Commission characterized this classification change as "requiring the mailer on an annual basis to mail at least 5,000 pieces (instead of 600 pieces), or pay postage of at least \$100,000 (instead of \$12,000)." For clarity, the Postal Service notes that the eligibility criteria for GEPS contracts do not require the actual mailing of 5,000 pieces or actual payment of \$100,000; rather, the new criteria simply provide that the mailer must be *capable of* meeting those thresholds. A customer need not tender all of its mailable volume to the Postal Service: the competitive nature of the international shipping market is not amenable to such unilateral requirements by the Postal Service as a supplier.

Respectfully submitted,

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Statement of Supporting Justification

I, Frank Cebello, Executive Director, Global Business Management, am sponsoring this request that the Commission add the shell classification for Global Expedited Package Services (GEPS) contracts, filed as Docket No. CP2008-4, or the GEPS Contract filed as Docket No. CP2008-5 to the competitive products list for prices not of general applicability. This statement supports the Postal Service's request by providing the information required by each applicable subsection of 39 C.F.R. § 3020.32. I attest to the accuracy of the information contained herein.

- (a) *Demonstrate why the change is in accordance with the policies and applicable criteria of the Act.*

As demonstrated below, the change complies with the applicable statutory provisions.

- (b) *Explain why, as to market dominant products, the change is not inconsistent with each requirement of 39 U.S.C. § 3622(d), and that it advances the objectives of 39 U.S.C. § 3622(b), taking into account the factors of 39 U.S.C. § 3622(c).*

Not applicable. The Postal Service is proposing that the shell classification for GEPS Contracts be added to the competitive products list or, alternatively, that the GEPS Contract filed as CP2008-5 and offered in accordance with that shell classification be added to the competitive products list.

- (c) *Explain why, as to competitive products, the addition, deletion, or transfer will not result in the violation of any of the standards of 39 U.S.C. § 3633.*

Adding the shell classification for GEPS Contracts to the competitive product list will improve the Postal Service's competitive posture, while enabling the Commission to verify that each contract covers its attributable costs and makes a positive contribution to coverage of institutional costs. In turn, each successive contract under the shell classification will increase contribution toward the requisite 5.5 percent of the Postal Service's total institutional costs. Accordingly, no issue of subsidization of competitive products by market dominant products arises. The alternative proposal – that the GEPS contract be approved itself as a competitive product – would also improve the Postal Service's competitive posture, but to a lesser degree.

- (d) *Verify that the change does not classify as competitive a product over which the Postal Service exercises sufficient market power that it can, without risk of losing a significant level of business to other firms offering similar products: (1) set the price of such product substantially above costs, (2) raise prices significantly; (3) decrease quality; or (4) decrease output.*

When negotiating GEPS Contracts, the Postal Service's bargaining position is constrained by the existence of other shippers who can provide services similar to the Postal Service's. As such, the market precludes the Postal Service from taking unilateral action to increase prices or decrease service. GEPS Contracts concern volume-based incentives for the tendering of large volumes of Express Mail International (EMI) and/or Priority Mail International (PMI), both of which have been classified as competitive by virtue of their exclusion from the letter monopoly and the significant level of competition in their respective markets. As with EMI and PMI in general, the Postal Service

may not decrease quality or output without risking the loss of business to large competitors that offer international express and package delivery services. The relevant market also does not allow the Postal Service to raise prices or offer prices substantially above costs: rather, the contracts are premised on the offering of prices at a level that provides sufficient incentive for customers to ship specified volumes with the Postal Service rather than a competitor. If the Postal Service were to raise these prices, it risks losing these customers to a private competitor in the international shipping industry.

- (e) *Explain whether or not each product that is the subject of the request is covered by the postal monopoly as reserved to the Postal Service under 18 U.S.C. § 1696, subject to the exceptions set forth in 39 U.S.C. § 601.*

Because the underlying products, EMI and PMI, fall outside of the prohibition on private carriage of letters over post routes by virtue of the exceptions to the Private Express Statutes, neither are the GEPS Contracts subject to that prohibition. See part (d) above.

- (f) *Provide a description of the availability and nature of enterprises in the private sector engaged in the delivery of the product.*

See part (d) above. Private consolidators and freight forwarders also may offer international shipping arrangements whereby they provide express and package delivery services under similar conditions.

- (g) *Provide any available information on the views of those who use the product on the appropriateness of the proposed modification.*

The customer for this GEPS Contract is a business that plans to ship articles via EMI and PMI under the terms and conditions of the contract. This

customer has previously entered GEPS Contracts with the Postal Service pursuant to the latter's former authority, and it finds the arrangement sufficiently attractive to merit renewal. The Postal Service has concluded similar arrangements with numerous other businesses of comparable size, which indicates that the relevant segment of postal customers in general finds this type of product to be advantageous as against similar products offered by the Postal Service's competitors. Customers are aware that competitive services are provided by such private enterprises. However, no specific data are available to the Postal Service on GEPS Contract customer views regarding the regulatory classification of these GEPS Contracts as market dominant or competitive.

(h) Provide a description of the likely impact of the proposed modification on small business concerns.

The market for international express and package delivery services comparable to Express Mail International and Priority Mail International is highly competitive. Therefore, a shell classification for GEPS Contracts will likely have little, if any, impact upon small business concerns. Large shipping companies serve this market, particularly with respect to the volume customers represented by this and other GEPS Contracts; the Postal Service is unaware of any small business concerns that could offer comparable service for these volumes. By offering the prices in these GEPS Contracts, the Postal Service is giving the small business customers for these products an additional option for shipping articles internationally, as against the services offered by private industry competitors. Thus, the net impact on small businesses is positive, because of

the absence of negative impact on small business competitors and the positive impact on the small businesses with which the Postal Service has entered and will enter into these contracts.

- (i) *Include such other information, data, and such statements of reasons and bases, as are necessary and appropriate to fully inform the Commission of the nature, scope, significance, and impact of the proposed modification.*

The customer eligibility criteria for GEPS Contracts concluded under the Postal Service's previous authority included lower capacity thresholds, along the lines of the Postal Service's initially proposed Mail Classification Schedule language. The Postal Service recently published EMI and PMI price incentives for smaller customers that might have met the previous GEPS capacity thresholds. Because smaller customers are able to access these published prices without the need for a contractual vehicle, the prices provided in GEPS Contracts will be available only to customers capable of tendering a larger volume of qualifying items to the Postal Service. Therefore, the Postal Service proposes to modify the eligibility criteria for the GEPS Contract product classification to increase the capacity thresholds.