

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

COMPETITIVE PRODUCT PRICES
PRIORITY MAIL
PRIORITY MAIL CONTRACT GROUP

Docket No. MC2009-25

**REQUEST OF THE UNITED STATES POSTAL SERVICE
TO ADD PRIORITY MAIL CONTRACT GROUP
TO COMPETITIVE PRODUCT LIST
(May 19, 2009)**

In accordance with 39 U.S.C. § 3642 and 39 C.F.R. § 3020.30 et seq., the United States Postal Service hereby requests that Priority Mail Contract Group be added to the competitive product list within the Mail Classification Schedule.¹ This is a competitive product not of general applicability within the meaning of 39 U.S.C. § 3632(b)(3).² A redacted version of the Governors' Decision establishing the prices and classification and a certification of the Governors' vote is provided in Attachment 1.³ An unredacted version of the Governors' Decision is being filed under seal. Attachment 2 provides a statement of supporting justification for this request, as specified in 39 C.F.R. § 3020.32.⁴ Attachment 3 provides a certification that the price formulas are consistent with 39 U.S.C. § 3633, as required by 39 C.F.R. § 3020.32(c).

As explained in the supporting justification, the Postal Service believes that it is appropriate to add this contract group to the list of competitive products. The

¹ 39 C.F.R. § 3020.31(a), (c).

² *Id.* § 3020.31(d).

³ *Id.* § 3020.31(b) and (f).

⁴ *Id.* § 3020.31(e).

Commission should therefore approve this request as set forth in its rules. As required by 39 U.S.C. § 3642(d)(1), this Request is being published in the Federal Register. The Postal Service is also filing today five contracts within this group.

The Postal Service maintains that the portions of the Governors' Decision and accompanying analyses that contain information showing how prices are developed should remain confidential. The ability of the Postal Service to negotiate contracts would be compromised if such information were publicly disclosed. Also, public disclosure would compromise the ability of customers to negotiate favorable shipping services contracts in the future. The Postal Service is aware of no competitor or private company of comparable size and scope that releases similar information to the public.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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May 19, 2009

ATTACHMENT 1
to Postal Service Request
Docket No. MC2009–25

REDACTED GOVERNORS' DECISION

**DECISION OF THE GOVERNORS OF THE UNITED STATES POSTAL SERVICE ON
ESTABLISHMENT OF RATES AND CLASSES NOT OF GENERAL APPLICABILITY FOR
PRIORITY MAIL CONTRACT GROUP (GOVERNORS' DECISION NO. 09-6)**

April 27, 2009

STATEMENT OF EXPLANATION AND JUSTIFICATION

The Postal Service has entered into a number of domestic shipping services contracts over the past several months that provide for customized pricing and, in many cases, terms of service, for the contract partner's use of domestic competitive services. The services involved include expedited services (Express Mail® service and Priority Mail® service) and ground services (Parcel Select® service and Parcel Return Service®). Each existing contract has involved one or both of the expedited services, or one or both of the ground services.

Heretofore, we have established in a separate Governors' Decision the particular rates negotiated for each such contract and any changes in classification underlying those rates. The Postal Regulatory Commission has, at the request of the Postal Service in conjunction with receiving notice of our establishment of the rates and any classifications, added each of the contracts to the list of competitive products.

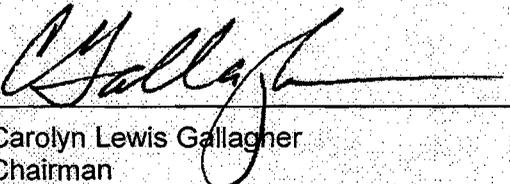
Based on our experience with these contracts, we have concluded that it would be appropriate to begin to streamline our process, beginning with Priority Mail contracts. Rather than establishing the particular rates for each Priority Mail contract in a separate decision, we are establishing in this decision a classification and rate formula that can be used by management to negotiate contracts for Priority Mail service. The classification would consist of contracts for the Postal Service to provide Priority Mail service to an individual customer at customized rates, as described in the draft language for the Mail Classification Schedule in Attachment A. Each individual contract will specify the applicable rates, any postage payment methods required, whether any volume

minimums apply, whether packaging is provided by the Postal Service, the length of the contract and any price adjustment mechanism, and any other customized terms or conditions applicable to the provision of Priority Mail service at the negotiated rates. The contracts are either to acquire new volume or when necessary to retain existing volume. The rates negotiated by management for each contract in the classification must result in a cost coverage between [REDACTED] and [REDACTED] percent, as calculated using the appropriate formulas in the analysis from management, which is contained in Attachment B. As explained in that analysis, such rates and classifications are consistent with the applicable statutory criteria set forth in 39 U.S.C. §§ 3632-3633.

ORDER

We direct management, in accordance with 39 U.S.C. § 3632(b)(3), to give notice to the Postal Regulatory Commission of, and to have published in the Federal Register, the rate and class not of general applicability which we establish herein. We also direct management to request that the Commission add the classification to the competitive product list in accordance with 39 U.S.C. § 3642. The rate formula and class set forth herein shall be effective on the day that the Commission issues necessary approval. As individual contracts are negotiated, management is directed to file appropriate notice and materials with the Postal Regulatory Commission in accordance with its rules of practice.

By The Governors:



Carolyn Lewis Gallagher
Chairman

MAIL CLASSIFICATION SCHEDULE

PART B—COMPETITIVE PRODUCTS

2000 COMPETITIVE PRODUCT LIST

NEGOTIATED SERVICE AGREEMENTS

Domestic

Priority Mail Contract Group 1 – This group consists of contracts for the Postal Service to provide Priority Mail service to an individual customer at customized rates. Each individual contract will specify the applicable rates, any postage payment methods required, whether any volume minimums apply, whether packaging is provided by the Postal Service, the length of the contract and any price adjustment mechanism, and any other customized terms or conditions applicable to the provision of Priority Mail service at the negotiated rates.

Analysis of Pricing Formulas for Priority Mail Contract Group

The implicit cost coverage for each contract will be at least [REDACTED] percent and will not exceed [REDACTED] percent:

$$\text{Cost Coverage} \geq [REDACTED] \text{ and Cost Coverage} \leq [REDACTED]$$

The cost coverage for the contract equals the contract's total revenues divided by its total costs, as follows:

$$\text{Cost Coverage} = \frac{\text{Total Contract Revenue}}{\text{Total Contract Cost}}$$

Each contract may have multiple price categories and negotiated components within Priority Mail. Examples of such categories or components would be Flat-Rate Boxes, Flat-Rate Envelopes, or Priority Mail Open and Distribute, whereby Priority Mail sacks containing other classes of mail are opened for further distribution at the destination facility. For contracts that include more than one category or component, the contract revenues and costs are weighted by the proportion of volume in each category or component, as follows:

$$\text{Total Contract Revenue} = \text{SUM of (Volume(cat}_i\text{) * (Unit Revenue(cat}_i\text{))}$$

$$\text{Total Contract Cost} = \text{SUM of (Volume(cat}_i\text{) * Unit Cost(cat}_i\text{))}$$

where cat_i is the i^{th} category or component covered by the contract, $\text{Unit Revenue}(\text{cat}_i)$ is the average revenue per piece and $\text{Unit Cost}(\text{cat}_i)$ is the average cost per piece for that category or component.

The revenue per piece for each category or component included depends on the negotiated price schedule and on the specific profile of pieces from the partner. The cost per piece similarly depends on the partner's profile. It is calculated as:

Unit Cost =

$$[REDACTED]$$

$$[REDACTED]$$

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Each cost element is inflated to reflect the appropriate time period.

So long as the estimated revenue from the contract equals or exceeds the total costs of the contract multiplied by the minimum factor of [REDACTED], the attributable costs will be covered (39 U.S.C. § 3633(a)(2)) and competitive products as a whole will comply with 39 U.S.C. § 3633(a)(3), which, as implemented by (39 C.F.R. § 3015.7(c)) requires competitive products to contribute a minimum of 5.5 percent to the Postal Service's total institutional costs. Accordingly, no issue of subsidization of competitive products by market dominant products should arise (39 U.S.C. § 3633(a)(1)).

**CERTIFICATION OF GOVERNORS' VOTE
IN THE
GOVERNORS' DECISION NO. 09-6**

I hereby certify that the Governors voted on adopting Governors' Decision No. 09-6, and that, consistent with 39 USC 3632(a), a majority of the Governors then holding office concurred in the Decision.



Julie S. Moore
Secretary of the Board of Governors

Date: 4-30-09

Statement of Supporting Justification

I, Mary Prince Anderson, Manager, Sales and Communications, Expedited Shipping, am sponsoring this request that the Commission add Priority Mail Contract Group to the list of competitive products. 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 the 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 this Priority Mail contract group 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.*

As indicated in the financial certification which follows, the services to be provided under the contract group will cover its attributable costs and make a positive contribution to coverage of institutional costs. The contract group 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 (39 U.S.C. § 3633(a)(1)).

- (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.*

Priority Mail service is provided in a highly competitive market. The Postal Service is unable to set prices substantially above costs, raise prices significantly, decrease quality, or decrease output, without losing this business to private competitors in the expedited shipping market.

In negotiating contracts under this group, the Postal Service's bargaining position is constrained by the existence of other providers of 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. As with Priority Mail services in general, the Postal Service may not decrease quality or output without risking the loss of business to competitors that offer similar expedited delivery services. The market does not allow the Postal Service to raise prices or offer prices substantially above costs; rather, the contract group is premised on prices and terms that provide sufficient incentive for the customer to ship with the Postal Service rather than a competitor.

- (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 189 U.S.C. 1696, subject to the exceptions set forth in 39 U.S.C. 601.*

I am advised that merchandise sent by Priority Mail services are not covered by these provisions. 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. Expedited shipping, similar to Priority Mail service, is widely available from well-known and successful private firms at both published and contract prices.

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

The customers whose contracts fall within this group support the addition of the contract to the product list so that the contractual terms can be effectuated.

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

The market for expedited delivery services is highly competitive and requires a substantial infrastructure to support a national network. Large shipping companies serve this market. The Postal Service is unaware of any small business concerns that could offer comparable service for this customer.

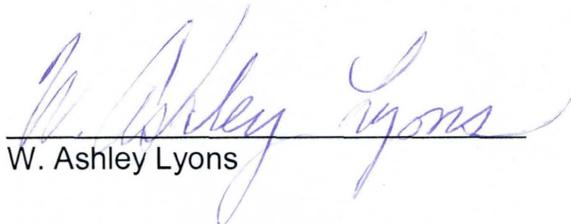
- (i) *Include such other information, data, and such statements of reasons and bases, as are necessary and appropriate to fully inform the Commission of the nature, scope, significance, and impact of the proposed modification.*

Additional details regarding the terms of the contract group have been provided to the Commission under seal due to the sensitivity of the terms to both customers and the Postal Service.

Certification of the Formulas for Priority Mail Contract Group Prices

I, W. Ashley Lyons, Manager, Regulatory Reporting and Cost Analysis, Finance Department, United States Postal Service, am familiar with the price floor and ceiling formulas for the Priority Mail Contract Group established in Governors' Decision No. 09-6.

I hereby certify that these formulas adequately represent all necessary cost elements. Contracts that offer Priority Mail services at set prices above the price floors will be in compliance with 39 U.S.C § 3633(a)(1), (2), and (3). The price floor formulas are designed to ensure that each contract covers its attributable costs, to preclude the subsidization of competitive products by market dominant products, and to make the requisite contribution to institutional costs.



W. Ashley Lyons