

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

Before Commissioners:

Ruth Y. Goldway, Chairman;  
Tony L. Hammond, Vice Chairman;  
Mark Acton;  
Dan G. Blair; and  
Nanci E. Langley

Review of Nonpostal Services  
(Phase II)

Docket No. MC2008-1

PHASE II REVIEW OF NONPOSTAL SERVICES UNDER THE  
POSTAL ACCOUNTABILITY AND ENHANCEMENT ACT



Washington, DC 20268-0001

January 14, 2010

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I. INTRODUCTION

A. Background

The Postal Accountability and Enhancement Act (PAEA), Pub. L. 109-435, 120 Stat. 3198 (2006), required the Commission to review nonpostal services provided by the Postal Service to determine whether they may be authorized to continue as nonpostal services, or should be terminated. 39 U.S.C. 404(e). The review was initiated in Phase I of this docket which culminated in Order No. 154.<sup>1</sup> In that Order,

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<sup>1</sup> PRC Order No. 154, Review of Nonpostal Services under the Postal Accountability and Enhancement Act, December 19, 2008. An appeal from Order No. 154 is pending. *United States Postal Service v. Postal Regulatory Commission*, D.C. Cir. No. 09-1032. For purposes of participating in this Phase II, the Postal Service presumes the validity of Order No. 154. See Initial Brief of the United States Postal Service, July 21, 2009 at 2 (Postal Service Brief).

14 services were authorized to continue as nonpostal services. Certain other revenue-generating activities were found not to be services of the Postal Service and therefore not subject to review. In addition, six Postal Service activities were determined pursuant to the PAEA to meet, for the first time, the definition of a postal service.

Three issues raised in Phase I were deferred to Phase II in order to obtain additional evidence. The first of the issues now before the Commission involves the licensing of Postal Service brands for use on products related to postal operations. In Order No. 154, the Commission authorized generally the licensing of products for promotional purposes, whether or not the products would be sold under the Postal Service brand. As a result of a filing by Pitney Bowes late in the Phase I proceeding, additional information was needed to review the Postal Service's commercial licensing of its intellectual property for USPS-branded products related to postal operations, which the Postal Service generally characterizes as mailing and shipping products. Order No. 154 at 75. Of those products, Pitney Bowes focused its objections on the retail sale under license of USPS-branded replacement ink cartridges for postage meters. *Id.* Pending the outcome of Phase II, the mailing and shipping products were grandfathered and permitted to continue in the interim without authority to execute new licenses relating to its operations. *Id.* at 76.

The second subject of Phase II concerns the Postal Service repair for compensation of equipment owned by others but manufactured by the same original equipment manufacturers (OEMs) as those manufacturing Postal Service equipment.

The third issue under review is the sale of unlicensed CDs and DVDs with questionable nexus to the Postal Service under the Postal Service's Officially Licensed Retail Program (OLRP). In Phase II, the Postal Service was also afforded a final opportunity to provide details about any additional revenue producing activities that may have been overlooked in its Phase I submittals.

## B. Summary of Order

This Order concludes Phase II and determines: that the licensing of Postal Service brands for use on mailing and shipping products related to Postal Service operations should be terminated in an orderly and timely manner; terminates the nonpostal service portion of the warranty repair program because it was not offered as of January 1, 2006, as required by 39 U.S.C. 404(e)(2); and authorizes the sale of CDs and DVDs only insofar as they are licensed by the Postal Service and otherwise comply with the requirements of the OLRP. CDs and DVDs may also be sold within packages of philatelic materials pursuant to the Philatelic Sales nonpostal service program authorized in Order No. 154.

The Commission finds the intent of section 404(e) is to concentrate the Postal Service's focus on its core responsibilities and away from nonpostal services that are not justified by a public need which can not be met by the private sector. A public need for third-party retailing of USPS-branded mailing and shipping supplies has not been demonstrated. Furthermore, any advantages of retailing mailing and shipping supplies under license are ameliorated by the success of the recently authorized postal service, ReadyPost, which offers essentially similar products at postal facilities throughout the country.

Based on the Postal Service's representations, the Commission has reviewed all of the Postal Service's revenue producing nonpostal activities undertaken as of December 19, 2006. Any additional revenue producing activities not brought before the Commission in this proceeding for review pursuant to section 404(e), are not authorized and shall be subject to further Commission proceedings pursuant to provisions of the PAEA.

### C. Procedural History

This Phase II proceeding commenced with a Commission order establishing procedures and providing opportunity for hearing.<sup>2</sup> The order provided an opportunity for the Postal Service to file sworn statements regarding the “details of each mailing and shipping service license and any additional information and evidence deemed relevant in support of its continuing the commercial licensing of products related to Postal Service operations.” *Id.* at 2-3. The Postal Service also was afforded the opportunity to provide details of its plan to expand its warranty repair program to other customers of its original equipment manufacturers, to identify the commencement date of such service, to quantify annual revenues from fiscal years 2006 through 2008, and to address the requirements of section 404(e) of title 39 and any other relevant matter. *Id.* at 3. Last, the order requested the Postal Service to develop a more complete record on its sale of CDs and the authorization for their sale, as well as any inadvertent omissions in Phase I for that retail program and, further, to indicate whether the Postal Service wishes to have the activity classified as a postal service or to continue to offer it as a nonpostal service. *Id.* at 4.

A direct case was submitted by the Postal Service on all three issues to justify Commission authorization of the three activities subject to review. The Postal Service offered as evidence the testimony of Gary A. Thuro regarding five contracts licensing mailing and shipping products.<sup>3</sup> Rick Osburn provided background on the warranty repair program expansion to repair equipment produced by OEMs but not owned by the Postal Service.<sup>4</sup> The Postal Service also submitted the testimony of Carrie A. Bornitz

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<sup>2</sup> Notice and Order Initiating Phase II Proceedings, January 9, 2009 (Order No. 168).

<sup>3</sup> Statement of Gary A. Thuro, November 17, 2008 (Thuro Statement); Supplemental Sworn Statement of Gary A. Thuro (amended March 30, 2009) (Thuro Supplemental Statement).

<sup>4</sup> Statement of Rick L. Osburn on Behalf of the United States Postal Service, January 29, 2009 (Osburn Statement).

describing the sales of music CDs and DVDs.<sup>5</sup> Additional material from Phase I also was designated for the record as part of the Postal Service's direct case.<sup>6</sup> The Postal Service's direct case was supported by declarations submitted by Randall E. Hooker on behalf of Pinpoint LLC, the Postal Service's licensee for postage meter replacement ink cartridges.<sup>7</sup> No party requested oral cross-examination or objected to entering the Postal Service's direct case into evidence and hearings on the direct case were cancelled.<sup>8</sup>

A rebuttal case was submitted by Pitney Bowes consisting of a declaration from Peter Wragg, Vice President of Merchandising of Pitney Bowes Inc., together with two attached exhibits and a library reference, objecting to licensing for sale USPS-branded ink cartridges. The declaration discussed the lack of a public need for, and the inappropriateness of, the Postal Service entering into the replacement ink cartridge market.<sup>9</sup> In response to Pitney Bowes' rebuttal case, the Postal Service submitted surrebuttal testimony concerning the Postal Service's approval processes for postage

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<sup>5</sup> Supplemental Statement of Carrie Bornitz on Behalf of the United States Postal Service (revised April 21, 2009), filed April 22, 2009 (Bornitz Supplemental Statement).

<sup>6</sup> See P.O. Ruling MC2008-1(Phase II)/5, April 17, 2009, entering these materials into the record. The material is comprised of introductory material on licensing previously filed, information regarding USPS Trademarks Used on Third Party Consumer Goods and Commercial Trademark Licenses, financial information for commercial licenses, and information regarding the five commercial licenses involving mailing and shipping supplies at issue in Phase II.

<sup>7</sup> Four Declarations of Randall E. Hooker on Behalf of Pinpoint LLC were filed October 29, 2008, November 7, 2008, November 21, 2008 and November 26, 2008.

<sup>8</sup> See P.O. Ruling MC2008-1(Phase II)/5, April 17, 2009.

<sup>9</sup> See Declaration of Peter Wragg in Response to Presiding Officer's Ruling No. 5, May 12, 2009; Library Reference PB-LR-1 is a sample USPS-branded postage meter replacement ink cartridge (Wragg Declaration).

meter systems and ink cartridges.<sup>10</sup> The record also includes Postal Service and Pitney Bowes responses to three Presiding Officer's Information Requests.<sup>11</sup>

No party expressed an interest in cross-examining the prepared responsive testimonies, and the scheduled hearings were cancelled.<sup>12</sup> Initial briefs and reply briefs were submitted by the Postal Service, Pitney Bowes, and the Public Representative on July 21 and July 31, 2009, respectively.

After briefs were filed, the Postal Service moved to reopen and supplement the record to enter the sworn supplemental declaration of witness Thuro regarding the Postal Service's termination of its agreement to license use of its trademarks on postage meter ink replacement cartridges by Clover Technologies Group, Inc., effective December 17, 2009.<sup>13</sup> By notice, Pitney Bowes responded that it "no longer has a direct and immediate interest in any of the specific licensing arrangements under consideration in Phase II." It further noted, "we continue to believe that review and oversight by the Commission of USPS licensing activities is required by the PAEA, see 39 U.S.C. § 404(e), and is essential as a consumer protection measure and as a means of protecting against unfair competition, especially where the Postal Service is offering licensed products in commercial markets over which it also exercises regulatory

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<sup>10</sup> Surrebuttal Testimony of Daniel J. Lord on Behalf of the United States Postal Service, July 6, 2009.

<sup>11</sup> See United States Postal Service Response to Presiding Officer's Information Request No. 1, April 3, 2009 (Response to POIR No. 1); United States Postal Service Notice of Revision to Its Response to Question 18 of Presiding Officer's Information Request No. 1, April 22, 2009; Pitney Bowes Inc. Response to Presiding Officer's Information Request No. 2, June 24, 2009 (Pitney Bowes Response to POIR No. 2); and United States Postal Service Response to Presiding Officer's Information Request No. 3, June 15, 2009 (Response to POIR No. 3).

<sup>12</sup> See P.O. Ruling MC2008-1 (Phase II)/7, June 5, 2009, and P.O. Ruling MC2008-1 (Phase II)/11, July 13, 2009.

<sup>13</sup> Motion of the United States Postal Service to Re-Open and Supplement the Record, November 18, 2009; Supplemental Sworn Declaration of Gary A. Thuro Regarding the Clover Technologies Group License Agreement, November 18, 2009.

authority.”<sup>14</sup> No party will be prejudiced by re-opening the record to accept this information. The motion is granted.

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<sup>14</sup> Notice of Pitney Bowes Inc. Regarding the Status of USPS-Branded Replacement Postage Meter Ink Cartridges and Postage Meter Supplies, November 19, 2009, at 1.

## II. LICENSING OF MAILING AND SHIPPING SUPPLIES

In Order No. 154, over Postal Service objection, the Commission determined that licensing of Postal Service intellectual property is “an ongoing, commercial activity offered to the public for purpose of financial gain.” Order No. 154 at 71. It is therefore a “service” as well as “nonpostal” and subject to review under section 404(e) of the PAEA. The service of licensing intellectual property was offered as of January 1, 2006, and therefore qualified for grandfathering pursuant to section 404(e)(2). *Id.* The Commission authorized the licensing of the Postal Service’s intellectual property such as stamp designs and trademarks for use on third-party consumer goods to continue as a competitive nonpostal service. *Id.* at 73.

The Commission rejected the Postal Service’s arguments that the PAEA does not contemplate licensing as a nonpostal service subject to review pursuant to section 404(e). Unless licensing is subject to section 404(e), the Postal Service through licensing could offer a wide variety of new nonpostal activities and circumvent the proscription against new nonpostal services, while avoiding Commission regulatory oversight of those services. *Id.* at 70. Although the Postal Service sought to distinguish its licensing from nonpostal services such as its OLRP where it sells licensed products directly to consumers, the Commission concluded the sale of licenses to market under Postal Service brands such as the Sonic Eagle is a service offering. *Id.* at 71.

Licensing of patents or stamp designs for promotional purposes meets the public need tests of section 404(e)(3). It serves a public need by not only generating revenues through the sale of promotional products and contributing to institutional costs, but by benefitting mailers in supporting the Postal Service’s universal service obligation. Licensing for promotional purposes also gives recognition to Postal Service brands in a way that can not be met by the private sector, which is unable to offer licenses to exhibit the Postal Service’s intellectual property. *Id.* at 73. Licenses unrelated to mailing and shipping products are uncontroversial and not an issue in this Phase II.

The licensing of Postal Service trademarks for use on commercial mailing and shipping products related to postal operations poses special issues inapplicable to the licensing of promotional products.<sup>15</sup>

The open question is whether the Postal Service may continue to license its trademarks to third parties so that they may produce and distribute “USPS-brand” products related to postal operations. This proceeding does not concern, and this Order does not restrict, the licensing of Postal Service trademarks for display on *other* brands of products relating to Postal Service operations to indicate compliance with specific Postal Service requirements, or fitness for use in preparing mail. For instance, the packaging of the Pitney Bowes brand replacement ink cartridge exhibits the trademark of a small Postal Service Sonic Eagle logo with the words “United States Postal Service” and the statement “An approved licensed vendor.” See Fourth Declaration of Randall E. Hooker, November 26, 2008, Attachment 1.

A. Grandfather Issue

The PAEA provides that only nonpostal services that were being offered to the public as of January 1, 2006 may continue to be sold. 39 U.S.C. 404(e)(2). The Postal Service points out that the Commission has already approved licensing its trademarks generally, as this was occurring January 1, 2006. *Id.* at 6. The Postal Service contends that the Commission should therefore authorize the licensing of its brands for use on

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<sup>15</sup> Licenses for use on products unrelated to postal operations may be continued.

mailing and shipping supplies (products relating to the use of the mails). Postal Service Brief at 5.<sup>16</sup>

Pitney Bowes argues that new licenses entered into after January 1, 2006 should be precluded. It believes the Order No. 154 holding that all licensing activities are nonpostal services and therefore eligible for approval under section 404(e) is overbroad and should be reconsidered. Pitney Bowes Brief at 9-10. Pitney Bowes opposes authorization of USPS-brand ink cartridges since they were not “offered” before January 1, 2006 and, therefore, not eligible to be grandfathered, and that other pre-January 1, 2006 licensing is “materially distinguishable.” *Id.* at 9. It distinguishes other licenses as a method for marketing the Postal Service brand that only the Postal Service can offer, not to promote a commercial product where market share can be taken from competitors serving the public need. Pitney Bowes also contends that authorizing all licensing would be inconsistent with the intent of the PAEA. The Commission should limit new licensing activities to “functionally equivalent” activities offered as of January 1, 2006, rather than permit new licensing that promotes a commercial product. *Id.* at 9.

Similarly, the Public Representative would have the Commission look beyond the shell activity (licensing) and review the actual activity to consider whether the Postal Service could directly enter the market where the licensed product will be sold. This

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<sup>16</sup> The Postal Service identifies five contracts as licensing mailing and shipping supplies. They are LePage’s 2000, Inc. (general mailing supplies)-January 14, 2005; Clover Technologies Group (ink cartridges)-November 26, 2007; Measurement Limited (scales)-July 18, 2007; U.S. Stamp and Sign (stampers, pads, embossers and mail preparation items)-February 12, 2008; and Deluxe Enterprise Operations (return labels)-March 11, 2008. See United States Postal Service Notice of Filing a Certification of Additional Information Related to the Licensing Program, re-filed May 11, 2009 (Thuro Additional Materials).

would effectively prohibit new licensing agreements related to postal operations entered into after January 1, 2006 as not meeting the PAEA's grandfather provisions.<sup>17</sup>

The Postal Service contends that individual licensing agreements are not separate “nonpostal services” for purposes of applying section 404(e). Pitney Bowes’ interpretation of the term “nonpostal service” would lead to illogical results. As one example posited by the Postal Service, if the term “nonpostal service” is applied at the individual transaction level, section 404(e) precludes the Postal Service from ever entering into a new lease of its real property. Postal Service Brief at 8.

*Commission analysis.* Pitney Bowes’ contention that each individual license is a separate nonpostal service is rejected. Order No. 154 determined that issue. See Order No. 154 at 71. The Commission determined licenses of a promotional nature meet the public need tests of section 404(e)(3). The Postal Service correctly points out Pitney Bowes’ argument that each individual license must pass the grandfather test would effectively nullify the Postal Service’s ability to enter into any new licensing agreements in the future. Postal Service Brief at 8. Even if, as the Public Representative suggests, the nonpostal service of licensing is segmented into promotional licenses and commercial licenses because commercial licenses relate to postal operations and thereby raise different issues requiring separate review, both types of license meet the PAEA’s grandfather requirements. The LePage’s 2000, Inc. contract licensing the sale of several mailing and shipping products was executed on January 14, 2005, well before January 1, 2006. As the Postal Service was offering commercial licenses for mailing and shipping products prior to the cutoff date, the grandfather provision is met by licenses for mailing and shipping products executed after that date.

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<sup>17</sup> See Initial Brief of the Public Representative, July 21, 2009, at 5-6 (Public Representative Brief). Under this theory, three of the five Postal Service licensing contracts for products related to postal operations would be barred because of their execution date. The LePage’s 2000, Inc. contract, was executed before January 1, 2006. Return mailing labels under license to Deluxe Enterprise Operations were marketed prior to 2006. See Thuro Additional Materials, second attachment, at 2.

B. Public Need—Mailing and Shipping Supplies Generally

Postal Service witness Thuro contends the commercial licensing program provides three benefits for the Postal Service: it leverages the Postal Service brand, enhances the Postal Service's image, and produces revenues that help support the Postal Service's core mission. Thuro Supplemental Statement at 4. In addition, the retail sale of these products provides consumer benefits which serve a public need. *Id.* at 5.

Relying on Order No. 154, the Postal Service says licensing which generates revenues and gives recognition to the Postal Service brand serves a public need. Postal Service Brief at 10. The value is demonstrated by the willingness of private sector licensees to compensate the Postal Service for its branded products indicating some public desire for the goods sold. *Id.*, Thuro, Supplemental Statement at 5; see *also* Response to POIR No. 1, question 11(g). Further, sale of mailing and shipping supplies in nonpostal retail outlets maintains a connection with the Postal Service that leverages the brand, adds convenience for customers, and facilitates and promotes the use of the mail by assisting in mail preparation. Retail sales of USPS-branded mailing and shipping products are more likely to generate a mailpiece for the Postal Service than a competitor. USPS-branded retail sales also increase the Postal Service's "footprint" and reassure customers of the durability, legibility and quality of the products. Thuro, Supplemental Statement at 4-5. In addition, the Postal Service asserts that if the Postal Service can sell similar products in its own facilities as postal services known as ReadyPost, it makes little sense to deny potential customers who are unable to make a trip to the post office the ability to purchase similar products at other retail locations. Postal Service Brief at 12.

The Postal Service's only argument to demonstrate the private sector can not meet the public need for licensing mailing and shipping products is that the Postal Service is the only entity that can provide this USPS branding connection, as

recognized by the Commission in Order No. 154 in authorizing promotional licenses. *Id.* at 10-11.

Pitney Bowes' arguments opposing the sale of USPS-branded replacement ink cartridges do not directly address the licensing of other mailing and shipping supplies, but two of its arguments are also applicable to other mailing and shipping products: (1) that USPS-branded products mislead consumers, and (2) the retail offerings of a government entity with related regulatory duties lead to unfair competition in the marketplace.<sup>18</sup>

Pitney Bowes also contends that activities that provide little contribution or merely defray costs do not meet the PAEA's public need test, and the Postal Service has not introduced evidence that Congress intended such an expansive reading of the public need test.<sup>19</sup> In such instances, the Postal Service is not seeking to fill a market void; rather, the Postal Service is looking for partners with an established track record and a presence in commercial channels. Section 404(e) was intended to permit nonpostal services only to fill an unmet consumer need and to avoid Postal Service behavior that distorts a mature market by taking away market share. *Id.* at 6-7.

Expressing concern with "potential market abuse and unfair competition" by the Postal Service, Pitney Bowes also opposes the Postal Service's competitive entry into markets where it would exercise a dual role as both competitor and regulator.

The Public Representative reiterates concerns that he expressed in Phase I regarding the trademark laws and the Postal Service's licensing practices. The Public Representative says Postal Service branding of mailing and shipping products confuses

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<sup>18</sup> Participant comments in Phase I expressed concerns that it is inappropriate for the Postal Service, rather than focusing on its core business, to leverage its own government "brand" to expand into virtually any business activity, thereby directly competing with private firms without adequate oversight. See Comments of Chamber of Commerce of the United States of America Responding to Order No. 126, November 19, 2008.

<sup>19</sup> Initial Brief of Pitney Bowes Inc., July 21, 2009 at 5-6 (Pitney Bowes Brief).

and deceives consumers, and he urges the Commission to ensure that consumers are not deceived by the Postal Service's branding of products related to postal operations. Public Representative Brief at 3-4. He argues the Postal Service should not be able to avoid oversight by doing through licensing what it could not do directly. *Id.* at 5. Finally, the Public Representative would require pre-implementation review of future licensing agreements to avoid potential confusion about the promotional or commercial nature of licenses. He contends this is necessary to allow the Commission to fulfill its oversight responsibilities. *Id.* at 7-8.

*Commission analysis.* 39 U.S.C. 404(e)(3) requires the Commission to consider the public need and the ability of the private sector to meet that public need, as well as other factors, before authorizing the Postal Service to continue licenses for mailing and shipping products. In Order No. 154, the Commission found promotional licenses meet the public need test of the PAEA. Upon review of this record, the public need for licensing mailing and shipping products related to postal operations has not been demonstrated.

In Order No. 154, in the context of licensing, the Commission addressed the various indicators of public need. Order No. 154 at 73. Licenses primarily of promotional value unrelated to postal operations meet the public need test for several reasons: they generate revenues and make a contribution to institutional costs, they benefit mailers, support the Postal Service's universal service obligation, and promote and give recognition to the Postal Service brand. *Id.*

To demonstrate public need for commercial USPS-branded mailing and shipping products, the Postal Service cites a series of potential benefits which it believes derive from the sale of these mailing and shipping products such as a satisfied consumer demand, consumer convenience, revenue contribution, Postal Service brand recognition, and image enhancement. Many of these benefits were found in Order No. 154 to support the finding of public need for licensing of promotional materials. *Id.* at 71-73. However, the claimed benefits are not sufficient to support a finding of public

need for licenses of a commercial nature to sell products related to postal operations. In this case, the suggested benefits are either without sufficient evidentiary support or mitigated by factors that are not applicable to promotional licenses reviewed in Phase I. In addition, some of Pitney Bowes' arguments to reject the licensing of ink cartridges also respond persuasively to the Postal Service's claim that there is a public need for all of its USPS-branded mailing and shipping products. Any benefits are outweighed by the disadvantages of selling USPS-branded products that can confuse consumers and disrupt markets. Furthermore, the licensing of products that are also regulated by the Postal Service raises a potential for unfair competition that is prohibitive.

The Postal Service points to the sales and revenues from USPS-branded consumer products related to Postal Service operations as indicators of public demand for those products.<sup>20</sup> Thuro, Supplemental Statement at 4; Postal Service Brief at 10. Certainly, demand for the product is one facet of public need. See Order No. 154 at 39. Revenue generation can be an indication of consumer acceptance of the product, but given the Postal Service's unique position as a government monopoly, with its duty to provide postal services and the resulting impact on consumer perceptions about USPS-branded products, revenues from licensing the USPS brand for use on mailing and shipping products can not be relied upon as representative of public need.

Pitney Bowes and the Public Representative arguments that consumer purchases of USPS-branded products related to postal operations is likely driven by misunderstanding on the consumers' part are persuasive. The USPS-branded packaging creates unwarranted expectations about the warranty behind the products. The unique governmental fiat of the Postal Service to provide postal services nationwide contributes to the demand experienced for these products.

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<sup>20</sup> Royalties from the LePage's 2000, Inc. contract for sales of USPS-branded products in FY 2007 and FY 2008 were \$438,512 and \$354,860, respectively. The combined royalties from the other four contracts for FY 2007 and FY 2008 were \$14,553 and \$20,779, respectively. See Response to POIR No. 1, question 5.

Also, to the extent USPS-branded products displace private sector competitors' products, the recorded sales do not provide a clear indication of need for the USPS-branded products vis-à-vis competitors. The Postal Service has neither offered evidence nor alleged that its licensed mailing and shipping products differ in quality from other like products readily available in the marketplace. For instance, Pitney Bowes points out that there is no evidence USPS-brand postage meter ink replacement cartridges are any different from those already offered by Clover Technologies Group (Clover) in the market. Wragg Declaration at 5. As for the other USPS-branded mailing and shipping products, the USPS-branded products appear to be the same, if not identical to, those sold by competitors that are otherwise readily available in retail markets.<sup>21</sup>

Easier access to mailing and shipping supplies at nonpostal retail locations is claimed to be a convenience for customers. Thuro, Supplemental Statement at 5. But the ability to shop for USPS-branded mailing and shipping products at mass merchandise outlets adds little convenience for consumers who can, in this mature market, already purchase similar mailing and shipping supplies at those locations. Moreover, any incremental convenience of additional sources of supply for USPS-branded products is diminished by the fact that the Postal Service has been expanding its sales of mailing and shipping items as a postal service under the Postal Service's ReadyPost label and other labels at thousands of its facilities throughout the country as well as through its website. The ReadyPost postal service product was first introduced relatively recently in 2000, yet already packaging supplies are available in thousands of postal retail locations.<sup>22</sup>

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<sup>21</sup> For instance, the Postal Service lists the following licensed products: envelopes, bubble wrap, packing materials, foam sheets, mailers, tape, labels, notes, wrapping paper, postal scales, embossers, and address labels. See Response to POIR No. 1. Similar products offered by competitors are widely available in retail stores.

<sup>22</sup> See Docket No. MC2008-1(Phase I), Statement of Margot A. Myers on Behalf of the United States Postal Service, June 23, 2009 at 3 (Myers Statement).

The Postal Service suggests that it makes little sense to deny customers the opportunity to purchase USPS-branded products at retail facilities when they may be purchased at postal facilities. Postal Service Brief at 12. However, under the PAEA, the sale of packaging supplies such as ReadyPost as a postal service does not necessarily justify licensing the sale of similar supplies through retail stores. Although the sale of licensed products at retail stores in nonpostal locations and the sales of ReadyPost packaging supplies to customers in postal facilities are similar, the Commission's responsibilities when deciding whether to authorize postal, vis-à-vis nonpostal services, differ significantly.

A fundamental dichotomy exists within the PAEA between postal services such as the sale of ReadyPost packaging at post offices, and the nonpostal service of licensing Postal Service brands for use on retail mailing and shipping products. Under the PAEA, the former is a postal service rising to the level of a core business, the sales of which are directly managed by the Postal Service; the latter is a nonpostal service under the control of licensees and merchandisers which must be terminated unless, together with other factors, the Commission finds a public need for the service that the private sector is unable to meet.

The Commission has recognized "it is likely that most ReadyPost products are mailed." Order No. 154 at 33. As a postal service available at postal facilities, ReadyPost consists of shipping and mailing supplies designed to meet the public's immediate mailing needs. *Id.* For instance, items such as individual padded envelopes and boxes are sold through postal channels. Thuro Supplemental Statement at 3, amended March 20, 2009. Competitors sell those same products in retail stores. The additional availability at commercial retail locations of USPS-branded products that may be used for the mail will not add a notable degree of convenience for consumers.

The variety of mailing and shipping items necessary or useful for mailpieces is also cited as a convenience, *id.* at 5, but the current variety of USPS-branded mailing

and shipping products is not extensive and consists of commonly available mailing and shipping items. See Response to POIR No. 1, question 5.<sup>23</sup> Even if the product list is expanded substantially, there is no evidence that the variety would expand beyond mailing and shipping products currently available in retail stores. Unusual mailing and shipping products for which there is limited demand and which are not readily available elsewhere could be sold as a postal service by the Postal Service directly in its own facilities, including its website.

The Postal Service claims additional revenue from mailing and shipping supplies helps meet the public need for a financially sound Postal Service. While this is true, the royalty income from mailing and shipping supplies of approximately \$385 thousand in FY 2008<sup>24</sup> was dwarfed by ReadyPost revenue for FY 2007, booked at \$121 million.<sup>25</sup>

Witness Thuro's claim that the postal-branded mail items are more likely to generate mail for the Postal Service than for a competitor is speculative. Witness Thuro suggests a postal-branded "padded envelope" purchased in a retail outlet is "more likely" to generate a mailpiece for the Postal Service than a competitor. Thuro Supplemental Statement at 4. However, USPS-branded mailing and shipping supplies such as tape and boxes may, or may not, be utilized to send items through the Postal Service. The Postal Service has previously presented evidence that purchases of mailing and shipping supplies at a retail facility are much less likely to generate mail than purchases at a postal facility.<sup>26</sup> The volume of additional mailpieces that might be

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<sup>23</sup> In FY 2007 and FY 2008, royalties were received for bubble pouches and wrap, envelopes, foam sheets, Kraft wrapping paper, labels, mailers, packaging paper, security boxes, shipping boxes/cartons, sticky notes, stretch wrap, tape, displays with multiples of the above items, stampers and embossers, scales, and return address labels.

<sup>24</sup> See Response to POIR No. 1, question 5.

<sup>25</sup> See Myers Statement at 3.

<sup>26</sup> The Postal Service pointed out during Phase I the results of an independent survey of shipping supply purchasers to support the assertion that customers are significantly more likely to use ReadyPost purchases for mailing than a purchase of similar supplies at a major discount retailer. Myers Statement at 3-4.

generated to benefit the Postal Service because of the USPS brand is speculative and, in the absence of more complete supporting information, can be given little weight. *Id.*

The Postal Service also cites as indicators of public need the benefits that accrue to the Postal Service from marketing USPS-branded merchandise. These benefits are primarily those gained in marketing any brand: promotion of brand recognition, increasing the “footprint” of the brand, promoting the sale of tie-in products, and increasing revenue by offering an apparent assurance of quality with products that meet standards of “durability, legibility and quality.” Thuro Supplemental Statement at 5. In this way, marketing a brand maintains a consumer connection with the brand.

The benefits of increased brand recognition from marketing the USPS brand are accompanied by offsetting disadvantages; in particular, the USPS brand can mislead consumers about the extent of product warranty. Wragg Declaration at 4; Public Representative Brief at 3-5. Also, the entry of the government sponsored USPS brand into markets related to postal operations has the potential to disrupt mature and healthy markets.<sup>27</sup> Finally, when the Postal Service competes in a market where the Postal Service provides regulatory oversight of a product or system, there is the potential for unfair competition, an additional reason for rejecting authorization for the Postal Service to license such products. Wragg Declaration at 2-3.

Wragg contends that demand for USPS-branded mailing and shipping products is generated by the erroneous assumption that the products include the guarantee of the Postal Service. *Id.* at 5. Whereas the Postal Service logo on products such as tee shirts would not give rise to an expectation of product quality in consumers, the sale of commercial mailing and shipping products related to postal operations raises consumer expectations that the Postal Service stands behind the product. These sentiments are applicable to all USPS-branded mailing and shipping products. The Postal Service “is perceived as the authority on all mailing related issues.” Pitney Bowes Response to

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<sup>27</sup> Pitney Bowes Inc. Response to POIR No. 2, questions 7, 9, and 10a.

POIR No. 2, question 6. It is considered the most trusted government agency and, as such, consumers could reasonably expect the USPS-branded products to be a “superior product.” Wragg Declaration at 5. The brandings, packaging, and marketing of the Postal Service brand appear to cause consumers to believe that it is a Postal Service product. *Id.* at 4. From the consumers’ perspective, the Postal Service is essentially selling the mailing and shipping products. Therefore, the USPS brand “suggests a unique approval or ownership relationship that enhances the perceived quality” of the products in issue here. *Id.* at 4.

This consumer perception is also recognized by the Postal Service. Witness Thuro acknowledges that a postal-branded mailing and shipping product “offers customers some measure of reassurance” that the products meet the “Postal Service’s standards for durability, legibility, and quality.” Thuro Supplemental Statement at 5. The Postal Service and Pitney Bowes each believe that the Postal Service brand will have a positive effect on consumers’ views and that, “[i]n particular, with respect to mailing and shipping supplies, customers will likely assume a certain level of quality and expertise with respect to products that bear the Postal Service’s widely recognized and respected brand.” Response to POIR No. 1, question 11(g); Pitney Bowes Response to POIR No. 2, question 6. Consumers will rely on the trademark that communicates the Postal Service is “standing behind the product.” *Id.*, question 5.

Nevertheless, the standard licensing agreement strives to protect the Postal Service from claims as to the quality or warrantability of the product. Wragg Declaration at 5. The Postal Service believes that the assurance consumers feel is not backed up by any Postal Service product warranty. The licensee assumes the risks of product liability, whether they relate to purchasing, manufacturing, distribution, sale or

marketing. Thuro Statement at 4-5. The consumer is unable to discern these limitations by casually inspecting the product.<sup>28</sup>

The Postal Service indicates that it is working to modify packaging to indicate the “Product Guarantee” is the manufacturer’s rather than the Postal Service’s warranty. It believes that would be more desirable than permanently barring these types of licensing agreements. Postal Service Brief at 12. Clarifying the guarantee on the packaging might reduce somewhat the misunderstanding in the minds of consumers about this aspect of the product being purchased. On the other hand, confusion over the product warranty, while significant, is only one aspect of the difficulty with USPS-branded products related to Postal Service operations. Reducing confusion would not result in a showing of public need for these particular types of licenses. Products carrying the USPS brand that are not significantly distinguished from competitors’ products may be purchased in lieu of other competitive products simply because they carry that Postal Service brand label.<sup>29</sup> Regardless of the guarantee, the demand generated for the product will arise from the status of the Postal Service as a government entity with a monopoly to carry the mail. Thus, sale of USPS-branded products does not serve to demonstrate a public need for USPS-branded products.

The Commission finds that the minimal financial benefits indicating public need that accrue to the Postal Service from marketing its own brand are more than offset by

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<sup>28</sup> For instance, the Public Representative points out that the sample postal meter replacement ink cartridge in the record prominently displays the United States Postal Service brand but does not display the actual manufacturer. Only in extremely small print, almost unreadable, the package indicates it is an “Official Licensed Product.” The package also states “Our 100% Guarantee” without stating who is the guarantor. Public Representative Brief at 4; Library Reference PB-LR-1. The Public Representative concludes that customers can not perceive a difference between products sold by the Postal Service and those sold under license. Public Representative Brief at 5.

<sup>29</sup> Commercial licensees are willing to share revenue with the Postal Service out of a belief consumers will “be more inclined to purchase a USPS-branded product *because* the trademark communicates to the marketplace that *the Postal Service is standing behind the product.*” Pitney Bowes Response to POIR No. 2, question 5. (Emphasis in original.)

the cost of potentially misleading the consumer and causing confusion among the public.

Another factor weighing against a finding of public need for USPS-branded mailing and shipping products is evidence that entry of USPS-branded products into mature markets may be disruptive to the market and its participants. *Id.*, questions 7, 9 and 10a. Also, the “Postal Service’s dual role as regulator and competitor in the same commercial markets creates an inherent conflict of interest and potential for abuse and unfair competition.” Pitney Bowes Response to POIR No. 3, questions 1-4.

First, it is important to recognize that competition *per se* is not objectionable. The PAEA recognizes the Postal Service sells products competitively. See 39 U.S.C. 3633. Nonpostal services are no different in this regard. To date, there is no specific allegation of anticompetitive behavior. Pitney Bowes Brief at 7, n.4. Pitney Bowes has not experienced and is not aware of any delays in Postal Service approvals of postage meter systems or inks for cartridges or that the Postal Service is otherwise engaged in unfair competition or in conduct that may substantially reduce competition. Pitney Bowes Response to POIR No. 3, questions 1-4.

Nevertheless, the nature of the competition the Postal Service brings to the marketplace for mailing and shipping products can be unfair in several respects. Substantial commercial harm may result to private companies in the marketplace. For example, in the sale of ink cartridges, the Postal Service enjoys an advantage that places private sector companies at a “competitive disadvantage.” See Wragg Declaration at 1. In the ink cartridge market, the total market is relatively fixed and the Postal Service market share must come from existing suppliers’ markets that include “numerous generic remanufacturers” who do not have established markets and who would be disproportionately harmed. Pitney Bowes Response to POIR No. 2, question 7. In that market, the Postal Service and Pinpoint claim the Postal Service is not selling ink; that the Postal Service is merely Clover’s licensor who, in turn, contracted with

Pinpoint to manufacture the product in China and sell it under the USPS brand.<sup>30</sup> Introducing “government-sponsored competition” into a “mature and healthy private market” will “harm and distort this functioning private market” where the private sector is meeting the public need for replacement ink cartridges. *Id.*; see also Pitney Bowes Response to POIR No. 2, questions 7 and 9.<sup>31</sup>

While licensing for primarily promotional purposes does not engender unfair competition in the marketplace, commercial licenses related to the Postal Service’s operations will cause the type of impact on competition that Congress sought to eliminate in the PAEA. The Postal Service is a government agency having a monopoly over the carriage of the mail which gives it a perceived expertise over the packaging and preparation of that mail. By licensing its trademarks to third parties so that they can make and sell USPS-branded products related to postal operations, the Postal Service is effectively engaged in a commercial activity in direct competition with private firms which are necessarily deprived of the opportunity to compete on a level playing field; precisely the type of impact on competition that Congress sought to restrict in the PAEA when it limited the Postal Service to core activities, except where authorized after a

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<sup>30</sup> Pinpoint’s witness Hooker notes Pitney Bowes’ share of the market at 94-96 percent indicates that it holds a virtual monopoly and that the market is not competitive. He states that the Postal Service’s licensing for the ink cartridges does not represent the entry of another player in the market, but that Pinpoint is the relevant market player. Hooker Declaration, November 11, 2008, at 3, 6. He concludes, “There is no new competition in this market.” Hooker Declaration, October 29, 2008, at 3. If there is *no new* entry into the ink cartridge market, witness Hooker does not explain how a “more efficient supply channel for the end user” is accomplished. *Id.* at 4. Witness Hooker presents conflicting claims that the USPS brand entry increases competition where there is a virtual monopoly and, on the other hand, claims there is “no new competition in this market.” It is not responsive to the concern that USPS branding will disrupt mature markets.

<sup>31</sup> Pinpoint claims the Postal Service is not in the market and therefore that phrases such as the “introduction of government sponsored competition” and “it is inappropriate for the Postal Service to compete in commercial markets” misrepresent the facts. Hooker Declaration, November 21, 2008, at 2-3.

Pinpoint’s objections are not well taken. Whether or not the Postal Service is actually selling the ink cartridges, the USPS brand on products sold at retail implies to consumers that the Postal Service is selling the ink cartridges and competing in the market. The perceived entry of the Postal Service can harm and distort a mature market.

Commission finding of need that could not be met by the private sector. See Order No. 154 at 19 and 21.<sup>32</sup>

The trademark laws are intended to protect against confusion and deception. The need for consumer protection from deception is especially true where the trademark is used on goods directly related to the trademark owner's line of business. In that case, "the trademark conveys the impression that the licensor stands behind the product." *Id.* at 72. The consumer may well believe that licensed mailing and shipping products are being sold by the Postal Service.

### C. Ability of the Private Sector to Meet the Public Need

Even if there were a public need for these mailing and shipping supplies, the Postal Service has not demonstrated the private sector is unable to meet that need. There is no showing that the mailing and shipping products already widely available in retail outlets are not similar or even virtually identical to USPS-brand products. The USPS-branded products are sold in large chain stores where similar alternative products are available in the absence of the USPS brand.<sup>33</sup>

Two other benefits claimed from USPS-brand mailing and shipping products are the assistance provided to individuals to prepare mail and the potential for an

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<sup>32</sup> "The dual concerns that emerged were a need to protect mailers from underwriting nonpostal activities through the postal monopoly and to ensure a level playing field in nonpostal markets entered by the Postal Service." *Id.* at 19. "Clearly, nothing in the PAEA or the history of postal reform suggests that Congress contemplated providing the Postal Service with a loophole to continue to engage in the same activities which caused Congress to bar all such future activities in the first place." *Id.* at 21.

<sup>33</sup> For instance, postage meter ink cartridges are available in nationwide office supply stores as well as "hundreds of office supply web-sites featuring dozens of generic and private label postage meter replacement ink cartridges." Wragg Declaration at 5. Exhibit 1 to the Wragg Declaration provides a "non-exhaustive" listing of websites indicating public access and the private sector ability to meet the need for ink cartridges. Many of those websites offer other mailing and shipping products such as tape and envelopes. In the absence of evidence to the contrary, there is no reason to believe that many generic and private label mailing and shipping products similar, if not identical, to those licensed by the Postal Service are not also widely available on many websites. In addition, the Postal Service's Postal Store website at [www.usps.com](http://www.usps.com) currently offers mailing and packaging supplies including envelopes, boxes, bubble mailers, bubble wrap, scales, rubber stamps and labels.

improvement in mail quality. Thuro Supplemental Statement at 4 *citing* tape, postage meters and scales. There is a benefit in assisting mailers and improving the quality of the mail. Nevertheless, the Postal Service has not shown these benefits can not be provided by the private sector. Competitors' products can also assist individuals in preparing items for the mail and in improving the quality of the mail. The Postal Service does not contend that its licensed USPS-branded mailing and shipping products (*i.e.*, envelopes, bubble wrap, packing materials, foam sheets, mailers, tape, labels, notes, wrapping paper, postal scales, embossers, and address labels) provide greater assistance or improve the quality of mail to any greater degree than other products in the marketplace. The USPS-brand products do not appear to excel in quality or include features not in products already available, nor do they appear to provide any special product improvements over those of competitors that would offer special assistance in preparing the mail or improving the quality of the mail. Padded envelopes cited as an example of products that assist in preparing the mail are generally available in the marketplace. See Thuro Statement at 4.

The USPS-brand package implies the USPS-brand product offers additional value as a result of the Postal Service's duty to provide nationwide mail service, and consumers may expect that, but additional value distinguishing USPS-branded mailing and shipping products has not been demonstrated. If the licensed mailing and shipping products do offer any improvement over competitors' products, the Postal Service has not presented that case. The Commission can not conclude that USPS-branded mailing and shipping products are sufficiently different from competitor products that the private sector is not able to meet the public need for these products.

The Commission concludes that the Postal Service has neither demonstrated a public need for licensing the Postal Service brands for use in mailing and shipping supplies, nor that the private sector does not have the ability to meet the public need for such products. Therefore, the Postal Service can not be authorized to license its

trademarks to enable a third party to sell USPS-branded mailing and shipping products related to postal operations.

*Termination of mailing and shipping licenses.* This Order requires the Postal Service to terminate the nonpostal service of licensing the sale of USPS-branded mailing and shipping products at retail locations other than Postal Service facilities.<sup>34</sup> Some similar packaging products, not sold under license, are sold directly by the Postal Service at its own facilities including its website. This decision regarding USPS-branded mailing and shipping products does not inhibit the Postal Service from enhancing customer convenience and its own revenues by utilizing its authority to provide postal services to expand the offerings at its postal facilities and its website.<sup>35</sup>

The types of packing supplies currently licensed as mailing and shipping products overlap some of the products offered as a postal service under the ReadyPost program. The Postal Service may wish to expand the ReadyPost program consistent with Commission rules to offer other mailing and shipping supplies at its retail facilities. However, new offerings not covered by the current MCS language would need to comply with the Commission's rules and supporting statements would need to be submitted pursuant to 39 CFR 3020.32.

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<sup>34</sup> The licensing of products unrelated to mailing and shipping is also included in some of the mailing and shipping contracts listed by witness Thuro. See Thuro Supplemental Statement at 2-4; see also LePage's 2000, Inc., U.S. Stamp and Sign, and Deluxe Enterprise Operations. This Order does not restrict those unrelated promotional products from being sold under the USPS brand because, among other reasons, the public need and demand for the products is not affected by the possibility that the consumer will assume particular Postal Service expertise in the area.

<sup>35</sup> The Postal Service filed proposed Mail Classification Schedule (MCS) language for shipping and mailing supplies as a competitive postal service product: "This includes Postal Service-branded packaging supplies currently offered under the ReadyPost registered trademark." It includes a generic line of shipping products and accessories and a decorative product line of shipping products. See Docket No. MC2009-19, Request of the United States Postal Service to Add Postal Products to the Mail Classification Schedule in Response to Order No. 154, March 10, 2009, Attachment A and Attachment F, Statement of Supporting Justification for Shipping and Mailing Supplies at 1. The Commission has approved MCS language for ReadyPost Service. Docket No. MC2009-19, Order No. 391, January 13, 2010.

*Termination of mailing and shipping product sales.* Noting that licensees have committed resources to manufacture and distribute products, the Postal Service requests that if the Commission terminates certain mailing and shipping contracts, it make the “order effective as of the contract termination date specified in the agreement.” Postal Service Brief at 18. The contract termination dates for mailing and shipping supplies vary significantly. According to the Postal Service, the LePage’s 2000, Inc. contract covering most of those products being sold under license does not terminate until 2017. Unless extended, other contracts terminate sooner.<sup>36</sup>

Permitting sales until 2017 would be inconsistent with the intent of the PAEA to order termination where the provisions of section 404(e) are not met. The Commission recognizes licensees may have committed resources to the manufacture and distribution of the products although, as discussed above, the products do not appear to be specially engineered for the USPS brand, and also are sold as other brands. To discontinue the offerings, only the packaging may need modification. Moreover, the licensees have been on notice of this proceeding at least since its inception in January 2008, and arguably from the date of the enactment of the PAEA in December 2006.

The Commission will balance the need to terminate these sales as soon as reasonable to avoid further potential for consumer confusion and market impact with the desire to mitigate potential economic loss to the licensees. The retail sale of these licensed mailing and shipping products shall terminate when inventories available as of the date of this Order are exhausted and in any case no later than December 31, 2010. If this creates hardship, the Postal Service may request that the Commission grant an extension of this date by filing detailed information explaining the circumstances.

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<sup>36</sup> The Postal Service has not submitted the LePage’s 2000, Inc. contract which may provide for an earlier termination date in the event Commission authorization is denied. The other contracts expire as follows: Clover Technologies, March 31, 2011; Measurement Limited, December 31, 2010; U.S. Stamp and Sign-September 30, 2009; and Deluxe Enterprise Operations-December 31, 2010. See Thuro Additional Materials.

### III. WARRANTY REPAIR PROGRAM

The Postal Service oversees a warranty repair program whereby original equipment manufacturers (OEMs) compensate the Postal Service for warranty repairs of equipment that the Postal Service purchased from the OEMs. In Phase I, the Postal Service identified this arrangement as associated with its equipment purchases.<sup>37</sup> In Order No. 154, the Commission determined that this rebate program reasonably may be characterized as part of the Postal Service's equipment purchasing arrangements rather than a commercial activity and, therefore, it was not a service subject to review under 39 U.S.C. 404(e). Order No. 154 at 84-85.

However, during Phase I, the Postal Service noted plans and the possible implementation of contracts to expand this program to repair equipment owned by other customers of the OEMs.<sup>38</sup> Order No. 154 recognized that this expansion of the warranty repair program may or may not be permissible under the PAEA and deferred this issue to Phase II to provide the Postal Service opportunity to justify continuing the activity as a competitive nonpostal service. *Id.* Pending conclusion of Phase II, the *status quo* was allowed to continue. Order No. 154 at 85.

Postal Service witness Osburn testifies that his department identifies this Postal Service equipment repair program as Fee for Service. Osburn Statement at 1. He states the overall program was initiated in 2004 when repair service to be performed by Postal Service contractors was first offered to "others", *i.e.*, OEMs contractually obligated to repair Postal Service equipment still under warranty.<sup>39</sup> All repairs are conducted by Northrop Grumman Technical Services under contract with the Postal Service on a straight pass-through price based on costs. The Postal Service is

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<sup>37</sup> Statement of Patrick R. Donahoe on Behalf of United States Postal Service, June 23, 2008, at 13 (Donahoe Statement).

<sup>38</sup> Donahoe Statement at 15. See *also* Initial Response of the United States Postal Service to Order No. 74, June 9, 2008, at 28-29.

<sup>39</sup> Response to POIR No. 3.

reimbursed by the OEMs for this charge, plus a markup retained by the Postal Service. Osburn Statement at 2. This provides revenue to the Postal Service. *Id.* at 3. Given its ongoing warranty repair program, the Postal Service proceeded to extend the activity to repair OEM equipment, owned by others, that is similar to equipment owned by the Postal Service. Revenue in FY 2008 was \$34,098. *Id.* at 3.

Consequently, “[o]n March 22, 2006, the Postal Service began offering the Fee for Service to other OEMs for non-postal owned equipment.” Response to POIR No. 3, question 1. Offers were made to OEMs with continuing obligations to repair equipment owned by others and “to other equipment owners.” Osburn Statement at 3. “One such offer was accepted by Royal Mail (United Kingdom)” to repair equipment in Kansas and “[s]imilar offers were extended.” Response to POIR No. 3, question 1. The Postal Service is reimbursed by others for repair of this equipment which is similar or identical to equipment that it owns. The Postal Service’s repair capabilities are “usually no longer available anywhere else” due to equipment age, redesign, and obsolescence and thus can be “absolutely necessary.” Osburn Statement at 3.

On brief, the Postal Service contends that this expansion of the repair offering to other owners of the OEM’s equipment does not alter the fundamental nature of the warranty repair program as an extension of the Postal Service’s purchasing arrangements. Postal Service Brief at 19-20. By providing warranty work for the OEMs of “a limited number of identical and/or similar Postal Service spare parts items,” the Postal Service says it is maintaining and improving its ongoing business contacts and relationships with its equipment suppliers and gaining insight into similar equipment from the same manufacturers who have a commercial interest in efficient repair of their equipment. Osburn Statement at 2. The service is not intended as a stand-alone commercial activity. It serves in a minor way to offset costs of the repair facilities in Kansas and Texas. *Id.* No other participant has commented on this issue.

*Commission analysis.* The first issue to address is whether the expanded activity is a new service, repairs for third parties; or, as the Postal Service suggests, part of its purchasing program. The Commission finds that expansion of the repair program by offering to repair equipment manufactured by the same OEMs, but owned by others, is a fundamental alteration from its purchasing arrangement with the OEMs and constitutes initiation of a separate commercial activity that is a nonpostal service.

Order No. 154 accepted as “reasonable” the Postal Service’s characterization that the warranty repair program which commenced in 2004 is essentially a purchasing arrangement rather than a commercial service for financial gain. The repairs discussed in Phase I were found to be part of a purchasing arrangement because they benefitted the OEMs from whom the Postal Service purchased its equipment by eliminating their need to move equipment, still under warranty, to a convenient location for repair. Also, the activity was not commercial in the sense that it was not offered in the marketplace.

Under the expanded program, the Postal Service is continuing to repair equipment manufactured by the OEMs, but the new activity is unrelated to its purchasing arrangements and is commercial in nature. The Postal Service is marketing the repair service for compensation to external owners of equipment and establishing new business relationships with the owners of the repaired equipment who have no direct relationship to the Postal Service’s purchasing arrangements. The repair centers were not established to repair equipment of external equipment owners, and the facilities will continue whether or not the Postal Service continues to provide this expanded repair service. Osburn Statement at 5. The repairs are unrelated to the core business of the Postal Service. The Postal Service, by marketing its services and collecting revenue from others for repair of particular types of specialized equipment, is engaging in an activity that must be characterized as a nonpostal service.

The further question is whether the expansion of the repair program to others was initiated prior to the January 1, 2006 cutoff date for continuing nonpostal services. The evidence clearly indicates, and the Commission concludes, that the nonpostal service was not offered until after the statutory deadline. Although the warranty repair program for in-house equipment was in existence before the January 1, 2006 cutoff date, the nonpostal service offering to repair equipment owned by others did not commence until March 22, 2006. Response to POIR No. 3, question 1.<sup>40</sup> The expanded warranty repair service therefore fails to meet the grandfather provisions of the PAEA and must be terminated.

To avoid unnecessary hardship to the Postal Service or owners of equipment with outstanding warranty repair contracts, if any, the authority granted in Order No. 154 to maintain the *status quo* until there is a final determination in this proceeding is terminated for all such contracts; except that authorization is extended to allow the completion of repairs on equipment owned by others currently at Postal Service repair facilities or in transit to those facilities. After the date of this Order, new nonpostal service repair contracts to repair equipment owned by others pursuant to the warranty repair program are not authorized.

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<sup>40</sup> This activity was continuing to be conducted on the date of enactment of the PAEA, December 20, 2006. The PAEA therefore provides for Commission review of this activity under section 404(e)(3).

#### IV. SALE OF CDS AND DVDS

In Phase I, the Postal Service submitted information about the sale of individual items of merchandise sold directly by the Postal Service under the OLRP.<sup>41</sup> Among the products listed was a Frank Sinatra CD promoting the Frank Sinatra stamp.<sup>42</sup> However, other popular music CDs offered for sale individually on the Postal Service's website did not appear to be related to the issuance of any stamp. *Id.* The Postal Service did not explain its legal authority for these sales and it appeared the Postal Service had neglected to seek authorization for these particular CD sales. Recognizing the scale of the Postal Service's operations, the Commission provided the Postal Service an opportunity to offer details of any omissions regarding its retail programs, including those related to CD sales. *Id.* Pursuant to the order initiating Phase II,<sup>43</sup> only the Postal Service supplemented the record about its sales of recorded music CDs and DVDs. No other participant commented on this issue.

Witness Bornitz states that since before January 1, 2006, the Postal Service tied the sale of CDs and DVDs to the release of certain popular stamps, seasonal events or as part of a mutual brand placement arrangement; for example, with a movie release when cross-branding includes Postal Service product placement.<sup>44</sup> Sales have occurred in retail lobbies and similar items are offered by the Postal Store at [www.usps.com](http://www.usps.com).<sup>45</sup> The witness also testified that she is not aware of any retail activities

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<sup>41</sup> See United States Postal Service Notice of Submission of Sworn Statement on "Nonpostal Services" Pursuant to 39 U.S.C. § 404(e), March 19, 2008, at 4.

<sup>42</sup> In Phase I, the Postal Service mentioned the sale of Frank Sinatra-themed song cards (greeting cards with musical chips) as not featuring "any Postal Service intellectual property." Myers Statement at 2.

<sup>43</sup> The order initiating this Phase II provided, "[t]o the extent it wishes to pursue this issue, the Postal Service shall file...complete details of each retail program for which information may have been inadvertently omitted in response to Order No. 74 and which the Postal Service seeks to have classified as a postal service or, alternatively, to continue to offer as a nonpostal service." Order No. 168 at 4.

<sup>44</sup> Bornitz Supplemental Statement at 3.

<sup>45</sup> The Postal Service plans to merge the merchandising strategy of these two outlets. *Id.*

not previously described in Phase I by Postal Service witnesses Lance and Myers in Phase I.

In this Phase II, the Postal Service contends that sales through its retail channels and website of CDs and DVDs relating to the issuance of a commemorative stamp, a postal theme, a seasonal event or mutual brand placement arrangement fall within the scope of its OLRP. Postal Service Brief at 22. As described by the Postal Service in Phase I of this proceeding, “This [OLRP] program provides for the sale of *licensed* retail merchandise in post offices. Licensees utilize postal trademarks and stamp images to develop products that can be sold in post offices.” (Emphasis supplied.)<sup>46</sup> The sale of OLRP as a nonpostal service was authorized in Order No. 154. Order No. 154 at 48-50. Pursuant to Commission order, the Postal Service filed proposed MCS language for the OLRP identifying the Postal Service’s sale of CDs as stamp-related or postal-brand-related merchandise.<sup>47</sup>

Postal Service testimony in this phase of the proceeding lists the few CDs and DVDs currently sold by the Postal Service at Postal Service retail locations, including its website, which it claims support the OLRP. Bornitz Supplemental Statement at 3. The offerings include DVDs related to a civil rights jumbo post card and the “Civil Rights Pioneer” stamp issued on February 21, 2009, as well as a DVD on civil rights history. A

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<sup>46</sup> Docket No. MC2008-1, Response of the United States Postal Service to Motion of the Public Representative to Compel Filing of Complete List of Nonpostal Services, April 1, 2008, Attachment Two. The witness in Phase I testifying about the OLRP program stated: “All OLRP items bear postal branding, trademarks, or other intellectual property, and roughly fall into two categories....” Statement of Tina M. Lance on Behalf of the United States Postal Service, March 19, 2008 at 11.

<sup>47</sup> The sale of CDs is included in the following proposed MCS language for the OLRP program filed by the Postal Service: Stamp-related or Postal-branded merchandise—stamp or postal brand-related merchandise includes items that have, or are associated with, a Postal Service issued stamp, or that have a postal brand. It includes ornaments, tote bags, CDs, framed artwork, and other types of merchandise. Docket No. MC2008-1, United States Postal Service Notice of Filing of Proposed Mail Classification Schedule Language for Six Nonpostal Services Pursuant to Order No. 120, November 7, 2008, at 6. The Postal Service omitted reference to DVDs in the proposed MCS language which it claims are also sold pursuant to this product category. This language was accepted provisionally into the MCS in Order No. 154 pending the conclusion of a Commission rulemaking establishing the form and content of rules for nonpostal services. Order No. 154 at 89.

Frank Sinatra CD supports the Frank Sinatra stamp. In addition, other CDs and DVDs are offered by the Postal Store on *www.usps.com* in support of stamp issuances. CDs support the Mancini and Gospel Singers stamps. DVDs support the Greetings from America and Benjamin Franklin stamps. *Id.* at 4.<sup>48</sup> Witness Bornitz claims the sale of the identified CDs and DVDs meets the same goals as the OLRP; they leverage the Postal Service brand, advertise and enhance the Postal Service's image, and the revenues help support the Postal Service's core mission. *Id.* at 5.

*Commission analysis.* In Order No. 154, the Commission determined that the Postal Service's OLRP and the philatelic program met the grandfather provisions of the PAEA and authorized those services to continue as nonpostal services.

The OLRP is, first and foremost, limited to the sale of licensed products. By definition, all OLRP products must be licensed by the Postal Service to qualify for sale under the OLRP. The licenses enable licensees to display postal trademarks and stamp images to develop products for sale in post offices and on the Postal Service's website.<sup>49</sup> The proposed MCS language specifies that OLRP products must also be stamp-related or postal-branded merchandise. As promotional material, the sale of such products is advantageous to the Postal Service and is encouraged.

To the extent CDs and DVDs meet the licensing and other postal-related requirements for sale under the OLRP, their sales fall under the OLRP umbrella as authorized products that may continue to be sold by the Postal Service. However, authorization does not extend to non-licensed CDs or DVDs simply because they are "related" to, or "associated" with, a stamp issued by the Postal Service. The Postal Service has issued stamps commemorating "love," "Christmas," and many individual

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<sup>48</sup> Retail locations normally discount inventory or return it to vendors, usually within three months after stamp issues are discontinued or removed from sale. Although no policy exists, remaining inventory on *www.usps.com* is sold or discontinued. Response to POIR No. 3, question 2.

<sup>49</sup> OLRP products fall into two categories: Ancillary Services consisting of postal branded items to assist mailers in using postal services and Brand Management consisting of items bearing a postal theme. Order No. 154 at 48-49.

performing artists. Virtually no limit would be placed upon merchandise sales under the OLRP if items did not have to comply with the licensing provisions of that nonpostal service.

The Postal Service has neither demonstrated nor represented that the CDs and DVDs sold as part of the retail program are licensed products displaying the trademark of the Postal Service. Given the parameters of the authorized nonpostal OLRP service, the sale of unlicensed CDs and DVDs under the OLRP is not permissible, even when they are related to postal stamps, postal themes, or events. Without the licensing requirement, many CDs and DVDs would qualify for sale under the broad additional requisite for the OLRP that merchandise must relate to a stamp, postal theme or seasonal event. For instance, the Postal Service's sale of "love" stamps might be cited as justification to sell any CD with romantic music, a large proportion of all recorded music and movies.

Additionally, the January 1, 2006 cutoff date for new nonpostal services provides clear instruction that Congress intended to prevent expansion of nonpostal services. A primary requisite of the OLRP nonpostal service is that retail merchandise must be licensed to utilize Postal Service intellectual property. To permit the unfettered sale of unlicensed CDs and DVDs would be tantamount to permitting a separate, new nonpostal service. Unless that separate nonpostal service is otherwise authorized, it is prohibited by the PAEA.

Although the sale of unlicensed CDs and DVDs may meet some of the goals of the OLRP, the sale of unlicensed CDs and DVDs is not proposed as a grandfathered a nonpostal service pursuant to section 404(e). The Postal Service has not claimed the sales are a separate nonpostal service nor has it demonstrated a public need for the Postal Service to sell CDs and DVDs that are not licensed by the Postal Service. Without adequate justification of public need as required by section 404(e), the

Commission can not authorize the Postal Service's sale of unlicensed CDs and DVDs as a separate nonpostal service.<sup>50</sup>

Nonetheless, it is apparent that some sales of CDs and DVDs fall within the scope of the philatelic program. According to the Postal Service, DVDs are packaged for sale with philatelic items such as stamps and other Postal Service images. For instance, the Postal Service currently lists certain DVDs, not under license, sold as a package in combination with philatelic materials. A DVD, "Milestones of the Civil Rights Movement," is sold in combination with 12 jumbo postcards of the 12 civil rights pioneers featured on a pane of stamps. Bornitz Supplemental Statement at 3-4. A DVD of "The States" is sold with a collector's pane of the "Greetings from America" stamps. *Id.* at 4. Also, a DVD of Benjamin Franklin is sold with a philatelic collection including an envelope with Benjamin Franklin commemorative stamps, a First Day of issue postmark and a special anniversary cancellation. *Id.* These sales packaged with philatelic offerings fall within the Philatelic Sales program.<sup>51</sup> These and similar philatelic "kits" for stamp collectors that include unlicensed CDs and DVDs are authorized if they are related to stamps, postal themes and postal events and sold in combination packages with philatelic materials.

In conclusion, Postal Service sales of unlicensed CDs and DVDs, even if related to stamps or USPS-branded merchandise, are not authorized for sale within the OLRP. However, CDs and DVDs specifically licensed by the Postal Service relating to stamps or USPS-branded merchandise are unique products that convey the advantages of licensed products sold under the OLRP and are authorized. In addition, the sales of CDs and DVDs related to stamps, postal themes and postal events in packages with

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<sup>50</sup> Furthermore, it seems highly doubtful that a persuasive showing could be made that the private sector could not meet any public need for additional outlets for sales of CDs and DVDs.

<sup>51</sup> The Postal Service's proposed MCS description for Philatelic Sales does not list the sale of CDs and DVDs as items included for sale under the program. See Docket No. MC2009-20, United States Postal Service Notice of Filing of Proposed Mail Classification Schedule Language for Nonpostal Activities in Response to Order No. 154, March 10, 2009, Appendix A.

philatelic materials are authorized as part of the Philatelic Sales program and may be continued.

## V. OTHER REVENUE PRODUCING ACTIVITIES

The Commission provided the Postal Service the opportunity in this proceeding to declare information about any other revenue producing activities it may have overlooked in Phase I and to present them for review in this Phase II. Order No. 168 at 4. Witness Bornitz indicates that her testimony is to provide information on any retail activities not discussed previously, and that she is not aware of any retail activities not specifically discussed in prior testimony in Phase I. All retail sales of merchandise, including recorded music, are intended to be covered by the description of the OLRP. Bornitz Supplemental Statement at 1. The Postal Service has not presented any other evidence of ongoing activities that produce revenue for the Postal Service. Accordingly, based upon the representations of the Postal Service that no such activities exist, the Commission concludes its review of all nonpostal services pursuant to section 404(e) of the PAEA.

## VI. ORDERING PARAGRAPHS

*It is ordered:*

1. The Motion of the United States Postal Service to Re-Open the Record and Supplement the Record, filed November 18, 2009, is granted.
2. The licensing of Postal Service branding of mailing and shipping products related to Postal Service operations for general retail distribution is not authorized and shall be terminated pursuant to section 404(e) of the PAEA as provided in the body of this Order.
3. That portion of the Warranty Repair Program, also known as the Fee for Services Program, to repair, for reimbursement, equipment of OEMs owned by others is a nonpostal service that was not offered as of January 1, 2006, and shall be terminated as provided in the body of this Order.
4. Only licensed CDs and DVDs that otherwise comply with the requirements of the OLRP are authorized for sale under the OLRP. CDs and DVDs may be sold as part of the Philatelic Sales program, a nonpostal service, if packaged with philatelic materials as provided in the body of this Order.

By the Commission.

Shoshana M. Grove  
Secretary