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POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268–0001

ANNUAL COMPLIANCE REVIEW, 2017	Docket No. ACR2017

REPLY COMMENTS OF THE UNITED STATES POSTAL SERVICE ON INBOUND LETTER POST
(February 27, 2018)

In Order No. 4323, the Postal Regulatory Commission (Commission) solicited comments on the Annual Compliance Report (ACR) of the United States Postal Service (Postal Service) for Fiscal Year (FY) 2017.[1] In Order No. 4395, the Commission extended the deadline for filing comments and reply comments related to Inbound Letter Post.[2] The Public Representative (PR) and SBE Council (SBE) filed comments related to Inbound Letter Post.[3] In these reply comments, the Postal Service addresses the principal concerns raised in those comments. As a threshold matter, it is significant to note that, even though the Postal Service does not concur with the limited analysis of only a subset of Inbound Letter Post revenues, nevertheless the PR ultimately emphasizes that she "***does not conclude that Inbound Letter Post is out of compliance with chapter 36 of Title 39***."[4]

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[1] Order No. 4323, Notice of Postal Service's Filing of Annual Compliance Report and Request for Public Comments, Docket No. ACR2017 (Jan. 2, 2018); United States Postal Service FY 2017 Annual Compliance Report, Docket No. ACR2017 (Dec. 29, 2017).

[2] Order No. 4395, Order Modifying the Procedural Schedule (Jan. 31, 2018). In the Reply Comments of the United States Postal Service filed in this docket on February 12, 2018, the Postal Service noted (at 3) that it would address the Public Representative's comments on Inbound Letter Post as part of the Postal Service's separate reply comments on this topic in accordance with the Commission's modified schedule.

[3] See PR Comments (February 1, 2018) at 22-26; SBE Comments (February 20, 2018) at 1-2.

[4] PR Comments at 26 (emphasis added).

I. AN EFFECTIVE ASSESSMENT OF COST COVERAGE FOR INBOUND LETTER POST MUST INCLUDE VOLUME FROM NEGOTIATED AGREEMENTS AND ALL SOURCES OF SUPPLEMENTAL REVENUE FOR INBOUND LETTER POST.

The Public Representative's analysis of cost coverage for Inbound Letter Post[5] omits significant portions of the revenue and volume associated with Inbound Letter Post, and thus fails to provide an accurate assessment of the entire financial portrait of Inbound Letter Post. The Postal Service receives revenue for Inbound Letter Post from numerous sources, including supplemental Universal Postal Union (UPU) remuneration for signature confirmation and tracking on registered items;[6] PRIME multilateral agreements (extra payments for tracking);[7] and negotiated rates under bilateral agreements;[8] in addition to base terminal dues, which are reported in the "Inbound Single-Piece First-Class Mail Int'l" category of the Cost and Revenue Analysis (CRA) filed with the ACR. The Public Representative's analysis evaluates only the revenue and cost data appearing in the "Inbound Single-Piece First-Class Mail Int'l" category of the CRA, which represents one subset of total Inbound Letter Post revenue. Similarly, although Inbound Letter Post volume is reported in both the "Inbound Single-Piece First-Class Mail Int'l" and "International Negotiated Service Agreements" categories of the CRA, the Public Representative's analysis considers only the volume reported in the

[5] PR Comments at 23-26.
[6] Mail Classification Schedule §§ 1510.2.2 (International Ancillary Services, Inbound International Registered Mail), 1602.5 (Negotiated Service Agreements, International, Inbound Market Dominant Registered Service Agreement 1) (Jan. 21, 2018) (available at https://www.prc.gov/mail-classification-schedule).
[7] Mail Classification Schedule §§ 1602.4 (Negotiated Service Agreements, International, Inbound Market Dominant Expres Service Agreement 1), 1602.6 (Negotiated Service Agreements, International, Inbound Market Dominant PRIME Tracked Service Agreement) (Jan. 21, 2018) (available at https://www.prc.gov/mail-classification-schedule).
[8] Mail Classification Schedule § 1602.3 (Negotiated Service Agreements, International, Inbound Market Dominant Multi-Service Agreements with Foreign Postal Operators) (Jan. 21, 2018) (available at https://www.prc.gov/mail-classification-schedule).

"Inbound Single-Piece First-Class Mail Int'l" category.

All of the sources of Inbound Letter Post revenue identified above relate directly to Inbound Letter Post volume, and should be considered Inbound Letter Post revenue for purposes of assessing the financial performance of Inbound Letter Post mail. The revenue reported in the "International Negotiated Service Agreements" category of the CRA is essentially letter post mail revenue enhanced by more favorable terms and conditions negotiated by the Postal Service. Some of this revenue, including revenue for tracking or registered services, enables the Postal Service to offer additional services or features for Inbound Letter Post volume that are considered desirable by mailers that purchase such services and features. Excluding this volume from the evaluation of Inbound Letter Post results in an incomplete evaluation of Inbound Letter Post.

Presumably, the reason the Commission developed the general rule that each negotiated service agreement is a "product" for evaluation of cost coverage for negotiated service agreements was to prevent the Postal Service from entering into financially unfavorable negotiated service agreements, and to give the Commission tools to enable it to issue remedies in connection with specific negotiated service agreements that failed to cover their costs.[9] Yet those same norms do not work well for compliance reviews of negotiated service agreements for Inbound Letter Post because, up until Calendar Year 2018, bilateral agreements for international market-dominant products have generally been used not for rate discounting, but rather generally for purposes of raising rates, as the Commission is aware from its review of such

[9] *See* Order No. 26, Order Proposing Regulations to Establish a System of Ratemaking, Docket No. RM2007-1 (Aug. 15, 2007), at ¶¶ 2087, 2088, 2092.

agreements. In sum, it makes more sense to consider inbound revenue from all sources for Inbound Letter Post, rather than using a patchwork approach not designed for the peculiarities of international letter post mail.

For the reasons described above, an accurate assessment of Inbound Letter Post for purposes of determining compliance with Chapter 36 of Title 39 requires the consideration of all sources of Inbound Letter Post revenue and volume. Inbound Letter Post revenue sources include supplemental UPU remuneration for signature confirmation and tracking on registered items, PRIME multilateral agreements, and bilateral agreements, in addition to base terminal dues. Accordingly, the Commission should view the figures reported in the CRA, on which the PR relied (at 22-26), with the contextual understanding that the cost coverage reported for the "Inbound Single-Piece First-Class Mail Int'l" category of the CRA is premised upon but a fraction of the true total revenues for Inbound Letter Post.

II. U.S. PARTICIPATION IN THE UNIVERSAL POSTAL UNION MUST BE EVALUATED COMPREHENSIVELY TO DETERMINE WHETHER THE SYSTEM, WHEN CONSIDERED HOLISTICALLY, PROVIDES BENEFITS TO AMERICAN BUSINESSES AND THE U.S. ECONOMY WHICH OUTWEIGH ANY DETRIMENTS OF THE SYSTEM.

It is critical that any analysis of the U.S. participation in the UPU be comprehensive. Contrary to SBE's one-sided concerns regarding alleged harm to U.S. businesses from international rates and the UPU,[10] American consumers and many American businesses derive benefits from U.S. participation in the UPU, a fact that must be taken into account in any comprehensive assessment of the value of that participation. For instance, because of the reciprocal nature of the UPU terminal dues system, it is not useful to evaluate the performance of discrete components of inbound

[10] SBE Comments at 1-2.

market dominant international mail without consideration of the performance of outbound international mail. The Government Accountability Office ("GAO") [11] reported Postal Service findings that U.S. participation in the UPU terminal dues system resulted in net positive revenue for the Postal Service when bidirectional flows are considered together because revenue from outbound mail exceeded the inbound loss. And due to the negotiation of more favorable terminal dues at the most recent 2016 UPU Istanbul Congress, the Postal Service expects that the net revenue it receives from participation in the UPU terminal dues system will increase over the new 4-year UPU cycle that became effective on January 1, 2018.

The positive impact of the UPU terminal dues system extends beyond the mailers who utilize international services. The revenue received by the Postal Service via the UPU framework as a whole provides positive contribution to the funding of the United States postal system, to the benefit of domestic mailers, and provides essential funding for infrastructure and other costs that enable the Postal Service to fulfill its domestic universal service obligation to deliver mail to 157 million U.S. delivery addresses 6 days per week.

Any disruption to the current system for the international exchange of mail through the UPU would have a negative impact on American businesses and consumers that must be considered. A disruption would subject U.S. exporters to increased outbound international shipping rates due to the reduction or elimination of Postal Service competition with private carriers, and could reduce or even eliminate their access to certain markets. Currently, these exporters benefit from the ability to

[11] *International Mail: Information on Changes and Alternatives to the Terminal Dues System*, GAO-18-112, U.S. Government Accountability Office (Oct. 12, 2017), at 10-15.

send items throughout the world with affordable, universal service rates that result from floors and caps in the terminal dues system. For the U.S. consumer, the current system provides a one-stop, easy and affordable means of accessing almost the entire world's postal system.

Although SBE attempts to support its allegations of harm from the UPU terminal dues system by citing alleged differences in international and domestic pricing,[12] its statements regarding international and domestic rates reflect a misunderstanding of postal operations and services and a lack of awareness regarding differences in the features and shipping conditions for international and domestic products and services. In general, domestic products include far more features than international products, and involve more processing and handling operations performed by the Postal Service. These enhanced features and the related increased processing and handling result in higher costs for the Postal Service.

For example, the Postal Service does not incur the cost of maintaining a network for collection of foreign origin mail, thereby making it less useful to compare international rates to domestic published rates, which include the cost of collection. In addition, foreign origin mail can be presented in larger quantities or in bulk, which reduces processing and handling costs, and thus domestic single-piece published rates, which include the costs of increased processing and handling costs associated with single-piece acceptance and entry, do not serve as an appropriate point of comparison for international rates.

[12] SBE Comments at 1-2.

With respect to SBE's specific comparison of international and domestic rates,[13] its use of "new Flat Rate Box pricing that went into effect earlier this year on January 21st" is misleading and not indicative of rates commonly paid by American businesses. The average item transported from China to the U.S., if shipped domestically, could be mailed at a domestic packet or flat rate or, in some cases, a domestic letter rate, which are significantly less than the rate for a Priority Mail Flat Rate Box. In addition, most domestic mail is shipped through commercial and discounted rates, and only a small portion of domestic mail is mailed at the Flat Rate Box rate or other full domestic single-piece retail rates. Accordingly, SBE's comparative example of international and domestic rates does not reflect the range of options available to actual domestic and international mailers.

Finally, SBE's "ongoing concerns surrounding the procedures adopted by the … USPS … that … have created an unbalanced consumer market in which foreign business interests are promoted to the detriment of [U.S.] businesses"[14] and its perception that "Postal Service leadership [had not adequately instructed the State Department] to achieve pricing formulas that … [enable] revenue neutral results"[15] reflect incorrect assumptions about the Postal Service's role in the UPU negotiation process, and its power over rates offered by foreign posts. Section 407(c)(1) of Title 39 requires the Secretary of State to request the views of the Commission before negotiating a treaty that would establish a classification or rates, like terminal dues, for a

[13] SBE cites unspecified "reports[, based on new Flat Rate Box pricing that went into effect earlier this year on January 21st] indicat[ing] that shipping one parcel from China to some east coast U.S. destinations – at distances of 7,000 miles or more – would cost only $3.66 for USPS delivery[, but f]or shipping within the U.S., the same one pound package would cost at least $7.20." SBE Comments at 1.
[14] *Id.*
[15] *Id.*

market dominant postal product. Upon receipt of a request by the State Department under Section 407(c)(1), the Commission initiates a review process during which it evaluates whether such UPU treaty proposals are "consistent with the standards and criteria established by the Commission under [39 U.S.C. §] 3622" for market dominant products.[16] As part of this review process, the Commission solicits comments from any interested persons "on the general principles that should guide the Commission's development of views on relevant proposals, in a general way, and on specific relevant proposals."[17] Those "general principles" can include, for example, the primary U.S. policy that Congress codified concerning international postal arrangements, which is "to promote and encourage communications between peoples by efficient operation of international postal services and other international delivery services for cultural, social, and economic purposes."[18] The State Department is then constrained to ensure that resulting treaties are consistent with the Commission's views, unless the State Department identifies a foreign policy or national security interest sufficient to justify deviation from the Commission's recommendations.

Thus, SBE's comments (at 1) that "the Postal Service leadership" had not "adequately instructed" the State Department in advance of the UPU's 2012 adoption of the terminal dues in effect from 2014 through 2017 reflects a misunderstanding of both the process and the substance that created the terminal dues in effect during FY 2017. The Postal Service does not "instruct" the State Department; by statute, the Commission solicits comments from any interested person, and then the Commission itself expresses its views to the State Department, thereby guiding the State

[16] 39 U.S.C. § 407(c)(1).
[17] 39 C.F.R. § 3017.3(a).
[18] 39 U.S.C. § 407(a)(1).

Department's treaty negotiations. The Commission employed this process prior to the 2012 UPU Congress in Doha. Thereafter, in its statement of views to the State Department regarding the four-year terminal dues system for 2014-2017, the Commission concluded that all three of the main terminal dues proposals of the UPU's Postal Operations Council were "consistent" with Section 3622 of Title 39, as they would improve cost coverage, create rate stability, enhance Postal Service revenues, better align terminal dues with domestic rates, and promote the establishment of just and reasonable rates.[19]

Though not at issue in the Commission's ACR 2017 docket, it is worth noting that the Commission again employed this statutory process in advance of the 2016 UPU Congress in Istanbul that produced the terminal dues in effect for 2018-2021. As in 2012, the Commission had the same statutory authority to constrain the State Department in its negotiation of the new terminal dues now in effect. However, after duly soliciting comments from any interested persons to help develop its views on the UPU terminal dues proposals, the Commission was equally split, 2-2 among the four Commissioners, and therefore the Commission did ***not*** advise the State Department that the main terminal dues proposals would be inconsistent with its regulations under federal law. [20] Absent any such constraint from the Commission, the State Department then exercised its primary jurisdiction and expert policy discretion in support of the terminal dues system that the UPU adopted for 2018-2021.

The likely consequences of a decision by the U.S. to exit the UPU, or refuse to accept the rates established in the Convention, are significant. A refusal to follow the

[19] Commission Response to Section 407(c)(1) Request for Views in connection with 2012 Universal Postal Union Congress in Doha, Qatar (Sept. 12, 2012), at 3-4, 7-9, 11.
[20] Notice of Posting of Views, Docket No. IM2016-1 (Oct. 7, 2016).

terms of the Convention, including the terminal dues provisions, could disqualify the U.S. from participation in the UPU system for the exchange of international mail. A decision by the U.S. Government to reject UPU terminal dues rates and withdraw from the UPU would create significant challenges for the Postal Service, and require costly and substantial changes in Postal Service operations that enable the exchange of international mail. With 192 members, the UPU facilitates the development of an international delivery network that is an important component of the U.S. economy. Without it, international service would be more expensive or difficult to offer on such a wide scale, simplified, and standardized basis. It is unlikely that a network created outside of the UPU framework would be as extensive, efficient, or affordable as the current network enabled by participation of the U.S. Government in the UPU. All of these factors must be considered in analyzing the U.S. participation in the UPU.

Further, the Postal Service has only limited control over the rates paid by foreign companies for foreign origin mail. The terminal dues paid to the Postal Service do not necessarily reflect the rates paid by foreign mailers abroad, and we expect that the rates of foreign posts, like those of the Postal Service, include the costs of providing acceptance services, overseas transportation, and other services.

As described above, the UPU terminal dues system for the exchange of international mail provides benefits to American consumers and businesses alike, and SBE's one-sided allegations regarding the impact of this system is inaccurate and reflects a misunderstanding of international and domestic products, rates, and operations.

Conclusion

The Commission should recognize, as the Public Representative expressly did in her Comments (at 26), that the special nature of Inbound Letter Post does ***not*** lead to a conclusion that the Postal Service is out of compliance with chapter 36 of Title 39. Not only is the Postal Service limited in its ability to change the base terminal dues themselves as the PR emphasized, but a myopic focus on inbound base terminal dues alone would be a disservice to both the Postal Service and the American public that it serves. Rather, the Commission should evaluate the net benefits of Inbound Letter Post holistically, as it is actually exchanged and remunerated in the real world. First, that means that all revenues that the Postal Service earns for Inbound Letter Post should be taken into account, including remuneration from supplemental features like registration and from negotiated service agreements for international letter post. Second, that means factoring the contributions of outbound letter post into any consideration of international letter post cost coverages, both because those same terminal dues benefit American mailers for exports and because Postal Service contracts are negotiated for bidirectional mail streams and rates. Third, that means understanding key differences from domestic mail, including the limitations constraining Postal Service control over international rates that the PR explicitly acknowledged. Fourth, that means fully weighing the overall benefits to American consumers and businesses from continued participation in the UPU.

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